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# RETIREE BENEFITS SECURITY ACT OF 1987

# HEARINGS

BEFORE THE

SUBCOMMITTEE ON
COURTS AND ADMINISTRATIVE PRACTICE

OF THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

FIRST SESSION

ON

## S. 548

A BILL TO AMEND TITLE 11, UNITED STATES CODE, THE BANKRUPTCY CODE, REGARDING BENEFITS OF CERTAIN RETIRED EMPLOYEES

APRIL 1 AND 24, 1987

Serial No. J-100-11

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# RETIREE BENEFITS SECURITY ACT OF 1987

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WEDNESDAY, APRIL 1, 1987

U.S. SENATE,
SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE,
COMMITTEE ON THE JUDICIARY,
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Howell Heflin (chairman of the subcommittee) presiding.

Also present: Senator Metzenbaum.

## OPENING STATEMENT OF HON. HOWELL HEFLIN, A U.S. SENATOR FROM THE STATE OF ALABAMA

Senator HEFLIN. The hearing will come to order.

This hearing will focus on S. 548, entitled the Retiree Benefits Security Act of 1987. This legislation was introduced by my colleague, Senator Howard Metzenbaum of Ohio, on February 19, 1987. I am pleased that we have been able to move quickly in response to the interest that this issue has generated.

This bill would make several changes in the bankruptcy law. First, it would amend section 1113(f) to title 11 of the U.S. Bankruptcy Code. This provision was enacted by Congress in 1984 to prevent the unilateral termination of rights guaranteed under a collective bargaining agreement by an employer seeking reorganization under chapter 11 of the Bankruptcy Code.

This amendment to section 1113 would clarify that the benefits protected under the collective bargaining agreement in section 1113(f) include the benefits of retired employees as well as those of active workers. The legislation also would add a new section 1114 to the Bankruptcy Code which would extend protection against unilateral termination or modification of retirement insurance benefits to all retirees without regard to whether or not they were covered by collective bargaining agreements. To provide for one class of retirees without making provisions for another is not only a distinction without a difference, but it was also a choice without justification.

The legislation would also provide with respect to all retirees that the employers can modify retiree insurance benefits in the absence of a negotiated settlement only if the court authorizes such modifications and when such modifications are necessary to enable the company to continue its business fairly and equitably to all parties.

The legislation further provides that the retirees should be treated as a separate class of creditors to strengthen the bargaining position of the retired employees. We have numerous union and corporate witnesses here today who will testify in support of this legislation, and they do so because they believe that this legislation is necessary to protect the rights of their workers and to guarantee not an extravagant life style for these workers, but a life style free of apprehension and uncertainty.

The retired employees who will testify today do so not from their technical expertise but from their real life experiences. Oftentimes on Capitol Hill, we make decisions in an isolated arena, and we never see the faces of the individuals and the lives that this legislation or any legislation touches.

Today, we have an opportunity to meet some of the individuals who have lived through the nightmare of the past 9 months. I commend the efforts of my colleague from Ohio for his tenacity, his perseverance, and for his swift response to the problems being faced by these retired employees.

We also are fortunate to have members of the American Bar Association and the American Bankruptcy Institute to testify before the subcommittee.

I might state at the outset that because of the need to move quickly on this legislation, some of the organizations are here specifically to accommodate our desire to understand and explore all facets of this legislation. Some of the witnesses would have preferred more time to study the legislation. It is incumbent on us as responsible legislators to hear from all sides of the issue and to understand the potential concerns of this legislation from different perspectives. So I personally would like to thank the ABA and the ABI for accommodating our expedited schedule.

Seldom is a perfect bill introduced, so the purpose of the committee process is to examine the legislation as fully as possible and to understand its impact.

I know that many of my fellow Alabamians were hurt when LTV filed for chapter 11 reorganization in July of 1986 when workers' insurance and medical benefits were terminated. While I can and do sympathize with the workers in Alabama and workers across the Nation, I realize that they alone fully comprehend the sheer frustration and terror of not knowing where the next dollar is coming from to feed the family or to pay the medical bills.

This is a very technical and complicated area of the law. Much interest has been generated by this legislation. We have, because of our desire to move quickly, already scheduled a second day of hearings on April 24. There are numerous requests to testify at today's hearing. I am sorry that we are not able to accommodate all of the witnesses who wish to testify on the first day.

To make the record as complete as possible, we will attempt to ensure that there is a balanced representation of all interests affected by this legislation.

I welcome my colleagues on the subcommittee. It is a pleasure for me to chair this Subcommittee on Courts and Administrative Practice. I welcome Senator Heinz and colleagues from the House and other witnesses who will testify today. I appreciate your coming and your willingness to participate.

We have statements from Senators DeConcini, Thurmond, and Grassley, along with S. 548, which we will insert into the record at this point.

[S. 548 and Senators' statements follow:]

II

100TH CONGRESS
1ST SESSION

# S. 548

To amend title 11, United States Code, the Bankruptcy Code, regarding benefits of certain retired employees.

---

IN THE SENATE OF THE UNITED STATES

FEBRUARY 19, 1987

Mr. METZENBAUM (for himself, Mr. HEINZ, Mr. GLENN, Mr. SPECTER, Mr. BYRD, Mr. LUGAR, Mr. RIEGLE, Mr. DURENBERGER, Mr. SIMON, Mr. ROCKEFELLER, Mr. LEVIN, and Mr. BOSCHWITZ) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

---

# A BILL

To amend title 11, United States Code, the Bankruptcy Code, regarding benefits of certain retired employees.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That this Act may be cited as the "Retiree Benefits Security Act of 1987".

SEC. 2. (a) Section 1113(f) of title 11, United States Code, is amended by inserting "(including any provision relating to benefits for retired employees)" after "provisions" the first place it appears.

(b) Section 1113 of title 11, United States Code, is amended by adding at the end thereof the following:

"(g) Claims arising under any collective bargaining agreement covered by this section, or as a result of the rejection of any such agreement, shall not be limited by section 502(b)(7) of this title.

"(h) The labor organization which is the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section is, for purposes of this section, the authorized representative of those persons receiving any retirement benefits covered by such agreement, unless such labor organization elects not to serve as the authorized representative of such persons.

"(i) In cases where the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section elects not to serve as the authorized representative of those persons receiving any retirement benefits covered by such an agreement, the court, upon motion of such persons, and after notice and hearing, shall appoint a committee of retired employees, from among such persons, to serve as the authorized representative of such persons, under this section.".

(c) Subchapter I of chapter 11 of title 11, United States Code, is amended by adding at the end thereof the following new section:

**"§ 1114. Payment of benefits to retired employees**

"(a) For purposes of this section, the term 'retiree benefits' means benefits for retired employees and their spouses and dependents, under any plan, fund, or program maintained or established in whole or in part by the debtor prior to filing a petition commencing a case under this title (through the purchase of insurance or otherwise) for the purpose of providing medical, surgical, or hospital care benefits, or benefits in the event of sickness, accident, disability, or death.

"(b) For purposes of this section, the term 'authorized representative' means the authorized representative designated pursuant to subsection (h) or (i) of section 1113 of this title, or, in the case of recipients of retiree benefits not covered by a collective bargaining agreement covered by section 1113, the authorized representative appointed pursuant to subsection (c) of this section.

"(c) The court, upon motion of recipients of retiree benefits not covered by a collective bargaining agreement covered by section 1113 of this title, and after notice and a hearing, shall appoint a committee of retired employees from among such persons to serve as the authorized representative of such persons under this section.

"(d)(1) Notwithstanding any other provision of this title, the debtor in possession, or the trustee if one has been appointed under the provisions of this chapter (hereinafter in this section 'trustee' shall include a debtor in possession), shall pay and shall not modify any retiree benefits to or for the benefit of retired employees and their spouses and dependents, except that—

"(A) the court, on motion of the trustee, and after notice and a hearing, may order modification of such payments, pursuant to the provisions of subsections (e), (f), and (g) of this section, or subsection (e) of section 1113 of this title, or

"(B) the trustee and the authorized representative of the recipients of those benefits may agree to modification of such payments,

after which such payments as modified shall continue to be paid by the trustee.

"(2) Any payment required to be made by any provision of this section after the date of the filing of the petition and before a plan confirmed under section 1129 of this title is effective has the status of an allowed administrative expense as provided in section 503 of this title.

"(e) With respect to retiree benefits that are not covered by a collective bargaining agreement covered by section 1113 of this title, the court, upon motion of the trustee, and after notice and a hearing, shall enter an order providing for modification in the payment of such retiree benefits, only if the court finds that—

"(1) the modifications in the retiree benefits sought by the trustee are necessary to permit the reorganization of the debtor and assure that all creditors, the debtor, and all of the affected parties are treated fairly and equitably; and

"(2) the balance of the equities clearly favors the entry of an order authorizing the trustee to modify the retiree benefits to the level sought by the trustee;

except that in no case shall the court enter an order providing for a modification lower than the level described in paragraphs (1) and (2).

"(f) With respect to retiree benefits that are covered by a collective bargaining agreement covered by section 1113 of this title, and only after such an agreement is rejected under such section, the court, upon motion of the trustee, and after notice and a hearing, shall enter an order providing for such modification in the payment of such retiree benefits as the court finds—

"(1) is necessary to permit the reorganization of the debtor and assures that all creditors, the debtor, and all of the affected parties are treated fairly and equitably; and

"(2) is clearly favored by the balance of the equities,

except that in no case shall the court enter an order providing for such modification which provides for a modification to a level lower than that proposed by the trustee in the proposal found by the court in the section 1113 proceeding to have complied with the requirements of subsections (b) and (c) of section 1113.

"(g)(1) Prior to a court issuing a final order under subsection (e) of this section, if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may authorize the trustee to implement interim changes in retiree benefits not provided by a collective bargaining agreement covered by section 1113 of this title.

"(2) Any hearing under this subsection shall be scheduled in accordance with the needs of the trustee.

"(3) The implementation of such interim changes does not render the motion for modification moot.

"(h) In calculating the amounts of the claims for unpaid future retiree benefits, or for any retiree benefits not provided due to modifications authorized pursuant to this section, and in calculating the amounts payable pursuant to any plan for such claims, any retiree benefits paid between the filing of the petition and the time a plan confirmed under section 1129 of this title becomes effective shall not be deducted or offset from such amounts unless otherwise agreed by the debtor and the authorized representative of the recipients of those retiree benefits.

"(i) No claim for retiree benefits shall be limited by section 502(b)(7) of this title.".

(d) Section 1122 of title 11, United States Code, is amended—

(1) in subsection (a), by striking out "subsection (b)" and inserting in lieu thereof "subsections (b) and (c)"; and

(2) by adding at the end thereof the following:

"(c) A plan shall place all claimants for retiree benefits (as such term is defined in section 1114), in a separate class consisting only of such claimants.".

(e) Section 1129(b)(2) of title 11, United States Code, is amended by—

(1) redesignating subparagraph (C) as subparagraph (D); and

(2) inserting between subparagraph (B) and subparagraph (D), as redesignated herein, the following:

"(C) With respect to a class of claimants for retiree benefits (as such term is defined in section 1114)—

"(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim, property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

"(ii) the plan provides that each holder of a claim of such class receive such value as found by the court to represent the minimum reduction in retiree benefits consistent with the ability of the debtor to provide such retiree benefits after confirmation of the plan.".

(f) The table of sections for subchapter I of chapter 11, title 11, United States Code, is amended by adding at the end thereof the following new item:

"1114. Payment of benefits to retired employees.".

(g) This Act and the amendments made by this Act shall become effective on the date of enactment of this Act and shall be effective with respect to cases commenced under chapter 11 of title 11, United States Code, in which a plan for reorganization has not been confirmed by the court as of October 2, 1986, and in which any retiree benefit, as defined in section 1114 of title 11, United States Code, is still being paid on October 2, 1986 or thereafter, and in cases that become subject to chapter 11, title 11, United States Code, after October 2, 1986.

○

## PREPARED STATEMENT OF SENATOR DECONCINI, A U.S. SENATOR FROM THE STATE OF ARIZONA

The topic that we address here this morning is one of vital importance to thousands of Americans, and one that will doubtless become important to thousands more in the future. The plight of those who have given the best years of their lives to LTV and other similar situated companies is a tragic consequence of the changing nature of our economy. It is ironic, and it is deplorable that in a country that has perhaps the highest quality of health care in the world, these people are often unable to live out their retirement years secure in the knowledge that our tremendous health care resources will be available to them in times of need. It is incumbent upon us in Congress to do something to resolve this situation.

At the same time, however, we must ensure that the integrity of the Bankruptcy Code is maintained. Throughout my Senate career, I have taken an active role in bankruptcy legislation, and I believe that we have developed a system that works pretty well most of the time. In particular, the chapter 11 process is one that we want to encourage for companies that are nearing collapse, but that are worth saving. In enacting legislation to protect retirees, we need to ensure that we do not upset the "delicate balance" that makes chapter 11 a success. I have not yet taken a position on the legislation before us today, and look forward to studying the views of both sides.

I would like to call particular attention this morning to the testimony of Mr. Richard Gitlin, president of the American Bankruptcy Institute. Dick is a nationally recognized expert in this area, and his contribution to the development of American bankruptcy law has been invaluable. The ABI is the largest organization of its kind in the country. It brings together creditors, debtors, and other interested parties in fashioning solutions to problems that arise in what has become an infinitely complicated area of the law. It is uniquely positioned to develop a solution to the problem that we address here today. I understand that the ABI has offered to work with Congress in solving this problem, and I urge my colleagues to give their offer serious consideration.

---

## PREPARED STATEMENT OF SENATOR STROM THURMOND, A U.S. SENATOR FROM THE STATE OF SOUTH CAROLINA

Mr. Chairman: Today the Courts and Administrative Practice Subcommittee of the Senate Judiciary Committee will receive testimony on the Retiree Benefits Security Act. The concerns which this legislation seeks to address are not new to Congress. Senator Metzenbaum and I worked together in the waning days of the 99th Congress to fashion a stopgap remedy for the problems raised for retirees by the impending bankruptcy filing of the LTV Corporation.

The law which passed is set to expire on May 15, 1987. This hearing, and one scheduled for later this month, are intended to examine the treatment of non-pension benefits for retirees under the Bankruptcy Code. The recent filing of petitions by companies with large numbers of retirees has brought this issue to the forefront. I look forward to working with Members of Congress in an effort to find a fair and equitable solution.

I would like to make three observations at the outset which I believe should set the foundation and the parameters for the debate. First, as I said when we passed the stopgap measure, section 1113 of the Bankruptcy Code was never intended to include retirees as part of the collective bargaining agreement between management and current employees. I was intimately involved in the negotiations that surrounded passage of the Bankruptcy Act of 1984, and no such interpretation was contemplated. Whatever Congress decides to do with respect to retirees' benefits, it should be understood that any pertinent bill will be an expansion, and not a clarification, of congressional intent with respect to section 1113 in 1984.

Second, any legislative initiative must protect the rights of all unsecured creditors in bankruptcy proceedings equally. If we focus on the concerns of some groups to the exclusion of others, we risk violating the very spirit of the Bankruptcy Code, which dictates that all affected parties be treated fairly and equitably. In this regard, I am concerned about the possible erosion of the integrity of the Bankruptcy Code through the creation of special exemptions which, though they seem justified today, will ultimately do damage to the overall effectiveness and fairness of the Code.

Third, any solution which Congress devises must not draw any distinction between the rights of union and non-union employees in a bankruptcy setting. Not only would this be contrary to the spirit of the Bankruptcy Code, but also it might put unintended pressure on employees with regard to their decision about union membership. I am not at all certain that the legislation before this committee preserves equal status for union and non-union employees at the present.

I would like to welcome the witnesses today, and I look forward to reviewing their testimony. I hope that the testimony of these witnesses and those in any future hearing will help the committee define the problem facing all unsecured creditors in bankruptcy proceedings so that we can consider a fair and equitable solution for all.

---

### PREPARED STATEMENT OF SENATOR CHARLES E. GRASSLEY, A U.S. SENATOR FROM THE STATE OF IOWA

Thank you Mr. Chairman. As my efforts in the last Congress in the area of bankruptcy proved to me, the reorganization of a business is a very complex legal undertaking.

Reading all of the sections of the Bankruptcy Code from front to back can lead one to a state of great intellectual confusion. This feeling is not limited to those who, like me, are not bankruptcy lawyers. In fact, I cite to you a passage from a famous bankruptcy case, *Bank of Marin* v. *England*, a 1966 Supreme Court case in which Justice Douglas remarked:

"We do not read these statutory words of the act with the ease of a computer . . . there is an overriding consideration that equitable principles govern the exercise of bankruptcy jurisdiction."

This is one of those times when I agree with Justice Douglas. I want to do what is equitable. When the bankruptcy law dealt our family farmers a bad hand, I sought to correct it last Congress. So it is with Senator Metzenbaum and this legislation.

I look forward to the testimony of the bankruptcy experts. We need guidance on how to craft a bill that's fair—to the retirees, to the company trying to make it, and to all the other innocent parties who are affected by a bankruptcy.

Senator HEFLIN. At this time I would like to call on Senator Metzenbaum to make any opening statement that he would like.

## OPENING STATEMENT OF HON. HOWARD M. METZENBAUM, A U.S. SENATOR FROM THE STATE OF OHIO

Senator METZENBAUM. Thank you very much, Mr. Chairman, for scheduling ~~a h~~earing so quickly on S. 548, the Retiree Benefits Security Act of 1987. I appreciate your understanding and support. This measure closes a gaping hole in our bankruptcy law which allows promises to retired workers to be disregarded at will.

Your opening statement, Mr. Chairman, indicates your understanding of the problem, your sympathetic willingness to consider this legislation, and I look forward to working with you and working with the ranking minority member of this committee, Senator Strom Thurmond, in connection with this legislation as well as every other member of the committee.

Nothing better demonstrates the need for quick action than LTV's unilateral suspension of retiree health benefits. On July 17, LTV filed for protection under our bankruptcy laws and suspended all retiree health and life insurance benefits in violation of its collective bargaining agreement and its contractual obligations.

In response to this callous action, Congress enacted a law securing these benefits through May 15. That legislation also prevents other companies from following LTV's terrible example, but an emergency measure is not enough. We must permanently amend the bankruptcy code to correct the balance. Retirees cannot, must not and should not remain at risk.

These people who gave so much of themselves, they were promised that in their retirement health and life insurance needs would be protected. But our bankruptcy laws tell retirees to stand at the end of the line. Promises to retirees are broken at the same time bankruptcy lawyer fees are paid, and in very substantial amounts, executive pensions were increased and the fund left almost totally depleted, and the banks are put at the head of the line. What kind of equity is that?

Those who built a company deserve better. They deserve to be treated fairly. They have earned that right. And this committee has a responsibility to see that they get it, and this Senate, this Congress, has an obligation to those retirees.

Mr. Chairman, in 1984 Congress amended the bankruptcy laws to require companies to honor their collective bargaining agreements. We worked on that law together. I remember our meeting and negotiating on that subject at 2:30, 3 o'clock in the morning, in the middle of the night, in order to bring about a bill and to get it enacted. Last year, Professor Vern Countryman, the Nation's most prominent bankruptcy expert, testified before this committee that what LTV did is "in flat violation of the 1984 law."

Two days after this committee received that testimony, the Senate passed my bill ordering LTV to reinstate retiree benefits. That evening, LTV went into court and requested an order to pay the benefits until January. Before adjourning last year, Congress adopted the Metzenbaum-Thurmond-Heinz amendment requiring LTV and other bankrupt companies to pay retiree health and life insurance benefits through May 15. This stopgap measure, as agreed to by Senator Thurmond, is intended to enable us to enact a comprehensive solution to this problem.

I want to parenthetically say that in the past I have had the privilege of working with Senator Thurmond in connection with expediting the passage of the two previous measures through the Senate. I look forward to working with him in connection with this measure. Hopefully we will have his support, and hopefully we will be able to pass the legislation promptly.

On February 19, I along with Senators Heinz, Glenn, Specter, Byrd, Rockefeller, Simon, Lugar, Riegle, Durenberger, Simon, Levin, Boschwitz, Sarbanes, Shelby, Bumpers, Inouye, and Mikulski introduced S. 548. Congressman Stokes, Congressman Traficant, and 70 cosponsors introduced an identical bill in the House, and I believe that my colleague from Ohio, Congressman Regula, is also a cosponsor of the House measure.

This measure clarifies the current meaning of the 1984 amendments, requiring companies to honor all their collective bargaining agreement obligations. Only after following the very detailed procedures in the 1984 law, including good-faith bargaining with the union, can the contract be modified.

Second, it moves health and life insurance benefits to the front of the line where they belong. It requires a company to continue paying for these benefits even after the termination of a collective bargaining agreement. Only if a company can prove a modification is absolutely necessary and that it treats everyone fairly can a court, after a hearing, order any modification.

Third, it protects the benefit payments as a company reorganizes and moves out of bankruptcy.

Mr. Chairman, retirees should not have to live in fear that their health benefits can be unilaterally terminated. They are not looking for a handout. They only want the bankruptcy lawyers to keep their hands off what they have earned. They deserve the protection S. 548 affords them.

If we are a caring nation, if we believe that our laws should reflect a sense of justice and compassion, then we can do no less.

I look forward to working with you, Mr. Chairman, and the other members of this committee to enact the best protections we can.

Senator Heflin. The record will stay open for opening statements by any other members of the committee. We have the highway bill that is on the floor, and some of them are at this time making statements pertaining to that. If they want to submit a statement later on this, the record will be open.

We are delighted at this time to have Senator Heinz. Senator Heinz, we will be glad to hear from you.

## STATEMENT OF HON. JOHN HEINZ, A U.S. SENATOR FROM THE STATE OF PENNSYLVANIA

Senator Heinz. Mr. Chairman, thank you very much. It is a pleasure to be before your committee and to appear with Congressman Jim Traficant and Congressman Ralph Regula with whom I have had an opportunity to work, both on this and other issues.

We are testifying, of course, on S. 548. That is legislation that Senator Metzenbaum and I and others have introduced to protect the retirees in chapter 11 bankruptcy.

Let me say, Mr. Chairman, we are here today because the LTV Corporation tried to end health benefits for 78,000 retirees when they filed for reorganization last July 17. And, Mr. Chairman, whether it is legal or not, I am not here to say, but LTV's attempt to stop payment on hospital bills for retirees—and, in some cases, already in the hospital—is nothing less than an outrage. We have got to change the law to prevent that kind of travesty from being repeated.

Now, let us look at what can and does happen under today's laws. A company, even one with cash and profitable subsidiaries, can escape into chapter 11 bankruptcy; then they can dump their retirees at the bankruptcy judge's door and then emerge profitable later with no further obligation to the retired employees who relied on the company's promises as a condition of their retirement. Frankly, it is inexcusable.

Now, LTV may not have entered into bankruptcy solely to cheat their retirees, but whether they did or not, they are paving the way for other companies that are looking for a way out of their retiree commitments. Without some deterrent, the rush to chapter 11 could become a serious problem in parts of this country where troubled manufacturing industries are now trying to fulfill commitments to retirees even though there may be two or three retirees for each active worker.

Chapter 11 may work for the troubled companies, and it may work for the major, usually secured, creditors. But it just does not work for the retirees. We need to recognize that retirees have an unusual and, I might say, especially vulnerable position in bankruptcy. We need to give the courts the statutory grounds to protect them.

Let me tell you three reasons why I think retirees are special and unique in bankruptcy. First, retirees are stunned when their company enters into chapter 11, and they are suddenly called "creditors," and their benefits are called "debts." Now, that is a funny thing to do to a type of compensation that we classify as deferred compensation. Other creditors, at least, knew that when they loaned money or when they sold goods to the company that the company owed them a debt. They knew there was a risk the company might never pay this debt, and they built that risk, usually, into the interest rate or into the price they charged.

In the case of retirees who, as employees, elected to defer compensation, either as health benefits or as retirement benefits, risk was never a factor they were taking into account in that retiree decisionmaking. And whether they chose to or were forced to retire, the retirees were often told that they would have those benefits not just until age 65, but for life. They could not, they would not have left their jobs without that security; most simply could not have afforded to retire without them.

The second difference is that these benefits are, as I am sure you know, Mr. Chairman, a literal lifeline to retirees. They are needed on a daily basis. Now, unlike bank creditors—and I have got nothing against banks—banks have reserves for losses. They may be able to survive for many years without the loan repayments—look what is happening in Latin America—until a reorganization plan is worked out. Well, retirees simply cannot afford to be without health coverage for years, or even a day, while the courts labor through chapter 11 proceedings. Even when retirees later get a cash settlement, what good is that to them if it comes after they need the medical treatment?

The fact is many retirees have had to defer necessary medical treatment when they lose their benefits, and they may be lucky to be alive or at least in good health when the courts finally get around to awarding them the cash.

The third major difference, Mr. Chairman, is that retirees are in a weak negotiating position with the company. Unlike the active workers and the major creditors, there is nothing that retirees have that the company needs. In fact, some companies are more likely to view retirees as some kind of an albatross. And to make it worse, the banks and in some cases the active workers may agree with the company. Some unions, like the steelworkers, will take action to protect the union retirees, but that is not always the case. We have seen cases where the union has declined to represent its retirees and where big bank creditors have threatened to force companies into liquidation if retiree benefits were not terminated. Retirees under current law are simply not equals in bankruptcy. What we have done in the current bankruptcy law is to get into the bus and go way to the back and not make any noise and see if they are ever told to get off.

Mr. Chairman, I think we ought to let the retirees ride in the front of the bus. They are not like the moneychangers that took their profits in a good year so they could weather the bad years. The retirees gave themselves to the company in the good years, and they made the good years good. In the bad years they deserve a measure of the security and dignity they earned.

Now, personally—and I think I speak for my fellow sponsor, Senator Metzenbaum—I think in our hearts we would like to go further than the Metzenbaum-Heinz bill. I know Jim Traficant would, too. Frankly, I would like to see us put a lien on the company for the benefits. Any time it promises benefits to retirees that are not funded, I would like to see that lien to retirees come prior to other secure debt when companies enter bankruptcy. I would like to see us prevent a company from terminating plans with unfunded benefits, whether they are in chapter 11 or not, as long as that company is still operating.

Now, that is pretty strong medicine, and I expect you would get a lot of criticism of that approach from the banks and other creditors. But that approach may be the only way to move the retirees all the way to the front of the bus where, in my judgment, they belong.

Now, S. 548 does not go that far, but it is a reasonable solution which is fair to all parties. It would at least prevent unilateral terminations of benefits, give retirees an equal voice in bankruptcy, and encourage companies and the courts to set up ongoing health and life coverage for retirees so they will not be left totally without health and life insurance coverage. Furthermore, it would do this without a major change in the structure of chapter 11 bankruptcy laws.

Mr. Chairman, I do hope that this committee will provide the protections we seek in S. 548. Without them, the threat to retirees across the country from chapter 11 bankruptcy is very troubling and very profound. And, further, I think that the continued use of chapter 11 by irresponsible companies as a way to dump their retirees weakens public confidence in the fairness of the bankruptcy process. In the end, public perception that chapter 11 is simply another corporate scam may force us all to reevaluate the underlying concepts of bankruptcy.

Mr. Chairman, I know these issues are of deep concern to you as well. I once again thank you for convening this hearing today. I would be happy to stay to answer any questions.

[The following material was submitted for the record:]

# STATEMENT OF SENATOR JOHN HEINZ
# BEFORE THE SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE, COMMITTEE ON THE JUDICIARY
APRIL 1, 1987

MR CHAIRMAN:

I APPRECIATE THIS OPPORTUNITY TO APPEAR BEFORE YOU ON S. 548, THE BILL SENATOR METZENBAUM AND I AND OTHERS INTRODUCED TO PROTECT RETIREES IN CHAPTER 11 BANKRUPTCY.

WE ARE HERE TODAY BECAUSE THE LTV CORPORATION TRIED TO END HEALTH BENEFITS FOR 78,000 RETIREES WHEN THEY FILED FOR REORGANIZATION LAST JULY 17. LTV'S ATTEMPT TO STOP PAYMENT ON HOSPITAL BILLS FOR RETIREES ALREADY IN THE HOSPITAL WAS AN OUTRAGE, MR. CHAIRMAN - WHETHER IT WAS LEGAL OR NOT. WE MUST CHANGE THE LAW TO PREVENT THAT KIND OF TRAVESTY FROM BEING REPEATED.

IT IS INEXCUSABLE THAT WE PERMIT COMPANIES TO ESCAPE INTO CHAPTER 11 BANKRUPTCY TODAY, TO DUMP THEIR RETIREES AT THE BANKRUPTCY DOOR, AND TO EMERGE PROFITABLE LATER WITH NO FURTHER OBLIGATION TO THEM. LTV MAY NOT HAVE ENTERED INTO BANKRUPTCY SOLELY TO CHEAT THEIR RETIREES. BUT THEY ARE PAVING THE WAY FOR OTHER COMPANIES THAT ARE LOOKING FOR A WAY OUT OF THEIR RETIREE COMMITMENTS. WITHOUT SOME DETERRENT, THE RUSH TO CHAPTER 11 COULD BECOME A SERIOUS PROBLEM IN PARTS OF THIS COUNTRY WHERE TROUBLED MANUFACTURING INDUSTRIES ARE NOW TRYING TO FULFILL COMMITMENTS TO RETIREES -- EVEN THOUGH THERE MAY BE 2 OR 3 RETIREES FOR EACH ACTIVE WORKER.

CHAPTER 11 MAY WORK FOR THE TROUBLED COMPANIES, AND IT MAY WORK FOR THE MAJOR AND USUALLY SECURED CREDITORS...BUT IT JUST DOES NOT WORK FOR THE RETIREES. WE NEED TO RECOGNIZE THAT RETIREES HAVE AN UNUSUAL AND ESPECIALLY VULNERABLE POSITION IN BANKRUPTCY, AND WE NEED TO GIVE THE COURTS THE STATUTORY GROUNDS TO PROTECT THEM.

LET ME TELL YOU WHY I THINK THE RETIREES ARE UNIQUE IN BANKRUPTCY. FIRST, RETIREES ARE SURPRISED WHEN THEIR COMPANY ENTERS INTO CHAPTER 11, AND THEY ARE SUDDENLY CALLED "CREDITORS" AND THEIR BENEFITS ARE CALLED "DEBTS". OTHER CREDITORS KNEW WHEN THEY LOANED MONEY OR SOLD GOODS TO THE COMPANY THAT THE COMPANY OWED THEM A DEBT. THEY KNEW THERE WAS A RISK THE COMPANY MIGHT NEVER PAY THIS DEBT - AND THEY BUILT THAT RISK INTO THE INTEREST RATE OR THE PRICE THEY CHARGED.

RISK WAS NEVER A FACTOR IN THE RETIREES DECISIONMAKING. WHETHER THEY CHOSE TO OR WERE FORCED TO RETIRE, THE RETIREES WERE OFTEN TOLD THAT THEY WOULD HAVE THESE BENEFITS FOR LIFE. THEY COULDN'T HAVE LEFT THEIR JOBS WITHOUT THAT SECURITY -- MOST SIMPLY COULD NOT HAVE AFFORDED TO RETIRE WITHOUT THEM.

SECOND, THESE BENEFITS ARE A LIFELINE TO THE RETIREES; THEY NEED THEM ON A DAILY BASIS. UNLIKE BANK CREDITORS, WHO HAVE RESERVES FOR LOSSES OR MAY BE ABLE TO SURVIVE FOR A FEW YEARS WITHOUT THE LOAN PAYMENTS WHILE A REORGANIZATION PLAN IS WORKED OUT, RETIREES CAN'T AFFORD TO BE WITHOUT HEALTH COVERAGE FOR YEARS, OR EVEN A DAY, WHILE THE COURTS LABOR THROUGH CHAPTER 11 PROCEEDINGS. AND EVEN WHEN RETIREES LATER GET A CASH SETTLEMENT - WHAT GOOD IS IT TO THEM WHEN IT COMES AFTER THEY NEED THE MEDICAL BENEFITS? THE FACT IS, MANY RETIREES HAVE TO DEFER NECESSARY MEDICAL TREATMENT WHEN THEY LOSE THEIR BENEFITS, AND THEY MAY BE LUCKY TO BE ALIVE WHEN THE COURTS FINALLY GET AROUND TO AWARDING THEM CASH.

THIRD, RETIREES ARE IN A WEAK NEGOTIATING POSITION WITH THE COMPANY. UNLIKE THE ACTIVE WORKERS AND THE MAJOR CREDITORS, THERE IS NOTHING THE RETIREES HAVE THAT THE COMPANY NEEDS. IN FACT, SOME COMPANIES ARE MORE LIKELY TO VIEW RETIREES AS AN ALBATROSS. AND TO MAKE IT WORSE, THE BANKS AND IN SOME CASES THE ACTIVE WORKERS MAY AGREE WITH THE COMPANY. SOME UNIONS - LIKE THE STEELWORKERS - WILL TAKE ACTION TO PROTECT THE UNION RETIREES - BUT THAT IS NOT ALWAYS THE CASE. WE HAVE SEEN CASES WHERE THE UNION HAS DECLINED TO REPRESENT ITS RETIREES, AND WHERE BIG BANK CREDITORS HAVE THREATENED TO FORCE COMPANIES INTO LIQUIDATION IF RETIREE BENEFITS WERE NOT TERMINATED.

RETIREES ARE NOT EQUALS IN BANKRUPTCY -- WE HAVE TOLD THEM TO RIDE IN THE BACK OF THE BUS.

MR. CHAIRMAN, I THINK WE OUGHT TO LET THE RETIREES RIDE IN THE FRONT OF THE BUS. THEY ARE NOT LIKE THE MONEYCHANGERS WHO TOOK THEIR PROFITS IN THE GOOD YEARS SO THEY COULD WEATHER THE BAD YEARS. THE RETIREES GAVE THEMSELVES TO THE COMPANY IN THE GOOD YEARS -- THEY MADE THE GOOD YEARS GOOD. IN THE BAD YEARS THEY DESERVE A MEASURE OF THE SECURITY AND DIGNITY THEY EARNED.

PERSONALLY, I WOULD LIKE TO GO FURTHER THAN SENATOR METZENBAUM'S AND MY BILL. I WOULD LIKE TO SEE US PUT A LIEN ON THE COMPANY FOR BENEFITS ANYTIME IT PROMISES BENEFITS TO RETIREES THAT AREN'T FUNDED. I WOULD LIKE TO SEE THAT LIEN TO RETIREES COME PRIOR TO OTHER SECURED DEBT WHEN COMPANIES ENTER INTO BANKRUPTCY. AND I WOULD LIKE TO SEE US PREVENT A COMPANY FROM TERMINATING PLANS WITH UNFUNDED BENEFITS - WHETHER THEY ARE IN CHAPTER 11 OR NOT - AS LONG AS THE COMPANY IS STILL OPERATING.

NOW THAT'S PRETTY STRONG MEDICINE. AND I EXPECT YOU WOULD GET A LOT OF CRITICISM OF THAT APPROACH FROM THE BANKS AND THE OTHER CREDITORS. BUT THAT APPROACH MAY BE THE ONLY WAY TO MOVE THE RETIREES TO THE FRONT OF THE BUS WHERE THEY BELONG.

S. 548 DOES NOT GO THAT FAR, BUT IT IS A REASONABLE SOLUTION WHICH IS FAIR TO ALL PARTIES. IT WOULD AT LEAST PREVENT UNILATERAL TERMINATIONS OF BENEFITS, GIVE RETIREES AN EQUAL VOICE IN BANKRUPTCY, AND ENCOURAGE COMPANIES AND THE COURTS TO SET UP ONGOING HEALTH AND LIFE COVERAGE FOR RETIREES SO THEY WON'T BE LEFT TOTALLY WITHOUT HEALTH AND LIFE INSURANCE. FURTHERMORE, IT WOULD DO THIS WITHOUT A MAJOR CHANGE IN THE STRUCTURE OF CHAPTER 11 BANKRUPTCY.

MR. CHAIRMAN, I HOPE THIS COMMITTEE WILL PROVIDE THE PROTECTIONS WE SEEK IN S. 548. WITHOUT THEM, THE THREAT TO RETIREES ACROSS THE COUNTRY FROM CHAPTER 11 BANKRUPTCY IS VERY TROUBLING. AND FURTHER, I THINK THE CONTINUED USE OF CHAPTER 11 BY IRRESPONSIBLE COMPANIES AS A WAY TO DUMP THEIR RETIREES WEAKENS PUBLIC CONFIDENCE IN THE FAIRNESS OF THE BANKRUPTCY PROCESS. IN THE END, PUBLIC PERCEPTION THAT CHAPTER 11 IS SIMPLY ANOTHER CORPORATE SCAM MAY FORCE US ALL TO REEVALUATE THE UNDERLYING CONCEPTS IN BANKRUPTCY.

I KNOW THESE ISSUES CONCERN YOU AS WELL, MR. CHAIRMAN, AND I THANK YOU FOR CONVENING THIS HEARING TODAY. I WOULD BE HAPPY TO ANSWER ANY QUESTIONS THE COMMITTEE MAY HAVE.

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RESPONSE OF SENATOR HEINZ TO QUESTIONS OF THE SUBCOMMITTEE ON THE COURTS AND ADMINISTRATIVE PRACTICE

1. Q. I am concerned about the future consequences of creating a special exemption for retirees from the Chapter 11 provisions of the Bankruptcy Code. Is your major interest protecting the benefits of retirees or amending the Bankruptcy Code? If you are interested in protecting the benefits of retirees, do you agree that we might consider ways of protecting them without resorting to amending the Code?

A. My primary objective is to protect the benefits of retirees. As I stated in my testimony, I do think we could provide more uniform protection to retirees if we could ensure that employers remain liable for their benefit obligations to retirees whether or not they reorganize or transfer assets and whether or not they seek the protection of Chapter 11.

One way to protect retirees without amending the Bankruptcy Code would be to require that employers arrange security for any benefit commitments to retirees that are not fully funded. In the event of reorganization, the assets securing the benefits would have to be transferred with the liability. In Chapter 11, the secured claims of retirees would stand prior to the claims of other subsequently-secured creditors, and retirees would be have a voice as secured creditors with veto power over reorganization. All of this could be accomplished without modifying the Bankruptcy Code. The problem with this approach is that it would require a major restructuring of benefits by all employers - very few of whom will ever enter bankruptcy.

Although solutions outside of bankruptcy might be conceptually neater, it is bankruptcy that creates unique problems of benefit insecurity for retirees. Contract law usually prevents employers in non-bankruptcy situations from reneging on their commitments to retirees. In bankruptcy, these contracts are typically rejected and the retirees have little legal recourse because of the protection accorded employers under Chapter 11. Short of requiring security for all unfunded benefit obligations, there is little Congress can do to protect retirees in bankruptcy that would not involve an amendment to the Bankruptcy Code.

The solution Senator Metzenbaum and I have proposed in S. 548 is intended to be very limited and reasonable. As I understand it, S. 548 would not change the standing of retirees relative to secured creditors, and it would not affect the existing priorities of most other claims. Retirees would still have only an unsecured claim for the present value of future promised benefits -- only current medical payments would have the priority of an administrative expense so that they could be paid in bankruptcy. Retirees would be represented and would have to approve the reorganization plan as a class, but they, like all other creditors, would have to accept what the court felt was reasonable.

2. Q. I am also concerned that the fundamental precept of the Bankruptcy Code, namely that all parties are treated fairly and equitably, is preserved. What safeguards do you believe are present in this bill to insure that all unsecured creditors are treated in a fair and equitable manner in a Chapter 11 proceeding?

A. I'm not sure I agree that retirees now get fair and equitable treatment under the Bankruptcy Code. They don't start out on a equal footing with other creditors. Their relationship to the company is unique among creditors in that the company is their only debtor. They have no reserves to absorb the loss or other debtor accounts to cushion them. Their ongoing need for health care cannot be met through a process in which health coverage is suspended and later reduced to a monetary award. Although they have an equal chance for monetary compensation, they are not compensated for the loss of the group health coverage or for the risk to their health during the bankruptcy proceeding.

Equitable treatment for retirees would require that their health coverage continue until reasonable alternative coverage can be arranged. S. 548 would not change the status of the retirees with regard to their claim for future health benefits - these would remain unsecured claims, to be valued and reduced on an equal basis with other unsecured claims - unless the court approved some other arrangement to continue their coverage. The only change would come in the treatment of the retiree's health benefits during bankruptcy - to ensure that they, like other unsecured creditors, would not have their health and livelihood jeopardized by the actions of their only debtor. While this might reduce the ultimate settlement to other unsecured creditors, it would protect retirees from the kinds of risks no other creditors face.

Senator **Heflin**. Do you wish to ask him any questions?

Senator **Metzenbaum**. No.

Senator **Heflin**. I do not believe I have any questions. If you would like to stay, it would be fine.

Congressman Ralph Regula, we are delighted that you are here, and we would be delighted to hear from you now.

## STATEMENT OF HON. RALPH REGULA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO

Mr. **Regula**. Thank you, Mr. Chairman. I want to commend you and Senator Metzenbaum for calling this hearing today to discuss this issue. I appreciate the chance to testify. My colleague, Senator Heinz, as well as your opening statements, clearly outline the problem.

We all know the challenges faced by the LTV retirees in the wake of the chapter 11 filing. Many people were put into a panic, having received terse letters from the company that their hard-earned benefits were being abruptly terminated. For many retirees, the loss of health and life insurance benefits left them without coverage or, for that matter, without the ability to buy coverage elsewhere.

It is unconscionable to jeopardize the benefits of America's retirees. These people have worked long and hard to earn these benefits, and they are not a gift to be withdrawn during hard times. America's retirees depend heavily on the security of health and pension benefits for their very lives, and to yank these benefits away works a terrible hardship on their financial, physical, and emotional health.

Companies should not be permitted to dip into pension funds whenever the going gets tough. These funds are not to be treated as a "slush" account to enhance a company's competitive position in the national and global marketplace. These funds should be considered sacred, to be used solely for the purpose for which they are collected—the payment of pension benefits.

I addressed these troublesome issues on February 5 of this year when I introduced H.R. 1040, along with other sponsors. This is a bill designed to protect the benefits of retirees of companies who file under chapter 11 and is similar to the bill introduced in both the Senate and the House that I have also cosponsored in the House.

My bill has two parts. First, it removes the May 15, 1987, cutoff date from the continuing resolution for the payment of retirement benefits, and instead requires the trustee in bankruptcy to ensure the payment of these benefits until they naturally expire under the terms of the original collective bargaining agreements.

Second, my legislation guarantees the benefits claims of retirees when a company files for reorganization under chapter 11. The bill secures the benefit claims, granting priority to these when a company's assets are distributed.

My bill and the one I have cosponsored with Congressman Stokes, similar to that of Senator Metzenbaum, addresses the very real issues that are being faced by the LTV retirees. They are not limited to LTV retirees, however, but, rather, extend protection to future retirees who find their former companies in bankruptcy court. This is a problem that goes beyond LTV.

In addition, through the Congressional Steel Caucus, on which I serve as the vice chairman, I have been involved with the Pension Benefit Guaranty Corporation in discussing changes in the funding requirements for maintaining pension funds in order to avoid an LTV situation in the future. And I think that is something that the Congress needs to address as to how that PBGC funding mechanism is structured, because we need to make sure that that fund is secure in the assets and that there is an adequate amount flowing in.

The PBGC is also proposing a variable funding mechanism which will not penalize responsible companies who have been providing adequate funding for their pension plans. This mechanism will ensure that responsible companies will not be forced to pay the lion's share of others, such as LTV's underfunded liability.

Again, I commend you for your initiative in conducting this special hearing today. Time is of the essence, and I appreciate the opportunity to appear before you.

[Responses to Senator Heflin's questions, subsequently submitted for the record, follow:]

### Responses of Congressman Ralph Regula to Senator Heflin's Questions

1. My legislation, H.R. 1040, seeks to permanently amend the bankruptcy code to grant priority to the unsecured claims of former employees when a company files under Chapter 11 of the bankruptcy code. It is my feeling that the claims of former employees are of substantial importance and should be legally afforded the protection they deserve when assets are distributed through the bankruptcy process.

2. My legislation places the unsecured claims of former employees in the fifth rank when assets are distributed under the bankruptcy proceedings. It is my feeling that this rank adequately and appropriately addresses these claims without superseding those claims which a court of law or the public interest would rightfully assess to be of more significance in distributing assets of a bankrupt company.

Senator Heflin. We will be delighted now to hear from Congressman Traficant.

## STATEMENT OF HON. JAMES A. TRAFICANT, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO

Mr. Traficant. Thank you, Mr. Chairman. I am very glad for the opportunity to come over here today to present testimony to your subcommittee here.

I would like to first start out by saying that our senior Senator from Ohio has led our Nation in attempting to help these retirees and all the people of Ohio and, specifically, my terribly impacted-upon district. I want to thank you and encourage you to continue on in that role.

Senator Metzenbaum. Thank you, Congressman.

Mr. Traficant. Specifically, of these 78,000 retirees, Mr. Chairman, almost 12,000 of them reside in my district. When LTV had taken their particular action, it was not that they attempted, in my opinion, to reorganize under the law that is granted for a company in such action. We are here today to talk about not the utilization of chapter 11 for reorganization, but the abuse of chapter 11. I believe Congress, the Senate and our Government has left open those tools for abuse.

Specifically, and I think this committee should perhaps, if necessary, review these facts, and I have asked for an investigation of LTV in the following areas, and one I believe the Senate should ensue with the power of their body. That specifically is this: No. 1, LTV gave early retirement packages to many people, including those who worked in my district.

Second of all, they came out and gave complete buy-outs to management personnel which depleted that pension fund. Then, subsequent to that, they came out and filed chapter 11. They aggregate those contracts of $400 supplemental, and for the first time in history they throw these payments out, medical and health benefits, completely—leaving these individuals to fare for themselves.

Now, let us talk about their representation. I believe at this point the law drives a wedge between the union and the retirees. The main concern of those steelworking unions in this case is to protect the current interests of those active employees. Now, I am not taking off on the unions because they have done an admirable job in trying to, within the context of the law, protect the interests of retirees. But nevertheless, the law serves an answer as a wedge to leave these retirees sitting out there almost by themselves.

So, specifically, there has to be a change in the law. I believe the legislative remedy offered by Mr. Metzenbaum and brought forward in the House is a good remedy. It speaks to those areas. In fact, it gives some priority by placing these individuals in the category where they are handled as an administrative expense.

However, the one area that I would like to see the bill go a little further—and I have introduced legislation 1488, and I am not to be misconstrued or misrepresented here today. I wholeheartedly support the Metzenbaum bill, and I would hope that the Senate would bring it forward, take it to the floor, and certainly pass it.

But if that bill in its present form would come to the House, I would be hoping that with the support of Senator Metzenbaum, who has evidently evaluated the climate here at the Senate, that we could expand upon it in one particular area; that is the area where modifications are present in the Metzenbaum bill.

The bill that I have presented, H.R. 1488, goes a step further. It says that no company, when filing for chapter 11, can reject any contract, whether executory or non-executory, that deals with retirees' medical, hospital and life benefits. I believe that that is the area that our Congress should be pursuing.

I am concerned about the modification clause, but I will say this: This bill brought forward by Senator Metzenbaum is a tremendous improvement for our retirees and would serve our country well.

Now, specifically, I want to put on record some of the dynamics of the human side of this tragic situation. A Mr. John Lipka in my district, when confronted with this tragedy, even though there was a temporary extension, thanks to the leadership of Senator Metzenbaum, he was so unsure of his future he committed suicide. I wonder if the people who are sitting in Congress today recognize the impact of the actions of LTV. I am not quite so sure yet that we do, and I believe our process is still searching rather than maybe a little bit more specifically directed.

So in closing out here today, I have a particular written statement that I would like incorporated into the record. I chose not to operate from that record, but I would just hope again that, No. 1, the Metzenbaum bill would be expedited and brought through the Senate; No. 2, that the Senate would listen to my request and consider asking for an investigation into the last-minute practices of LTV, when they, No. 1, granted those early retirement packages with supplemental, which I believe was the true intent to abrogate those policies in the chapter 11 action, and finally those buy-outs, total buy-outs of management people which led into almost $300,000, $400,000 per case which depleted the fund.

And, finally, I think Congress has to look ultimately at what Senator Heinz brought forward, the cash in profitable subsidiaries of some of these corporations when filing this chapter 11. Now, they have a good defense contract in the aerospace section, and I believe for Congress to let them run around making profit and to fly in the face of the tragic situation of our retirees and take the action they did is incongruent with our purpose here. Without question, I think we should address that, and hopefully legislation will strengthen PBGC. And, by God, before we spend more money all over the country if we have to, let us fortify PBGC; hopefully, that will be additional legislation that will come down the pike.

So, in closing, I would hope that these matters would be considered. I would hope that the Senate would look into the area of LTV as I have discussed and, if necessary, also support further strengthening in the House level and be considerate of that if, in fact, it can happen when it comes back for conference.

I am open for any questions that you have, and I thank you for giving me the opportunity to appear here today.

Senator HEFLIN. Without objection, your written statement will be made part of the record.

[The following material was submitted for the record:]

## TESTIMONY OF THE HONORABLE JAMES A. TRAFICANT, JR.

Mr. Chairman and Members of the Subcommittee, I appreciate this opportunity to testify before you today on behalf of the "Retiree Benefits Security Act of 1987". This legislation will give much needed assistance to those retirees who have been adversely affected by the recent LTV Corporation bankruptcy. This legislation will also go a long way in protecting the hard-earned benefits of other workers and retirees who may someday find themselves in the midst of a company bankruptcy.

Most of us here are very familiar with the events which have ultimately led us to this important hearing on this very important legislation. For this reason, I would like to only briefly comment on past events, namely the LTV bankruptcy, and then comment on situations that have resulted from that bankruptcy.

On July 17, 1986, the LTV Corporation filed Chapter 11 bankruptcy. At that same time, the company unilaterally terminated its retirees health, insurance, and hospitalization benefits. These benefits were terminated without the courtesy of prior notice. Because of a strike at the Indiana Harbor Works, these benefits were restored on July 26, 1986. Through court orders and emergency legislation, these benefits have been continued, and are slated to continue until May 15, 1987, as stated by law. Today we are here to discuss a legislative measure which would protect these benefits, as well as prevent similar situations from ever happening again.

It has been eight months since LTV declared bankruptcy. Since then, I have been actively involved in efforts, at both the local and federal level, to restore retiree benefits. The District which I represent, the 17th District of Ohio, is home to over 11,000 retirees who have been adversely affected by LTV's actions. These retirees spent their entire lifetime working for what we presently know as the LTV Corporation. Many are immigrants who were thankful to have a job. Most are veterans who served our country nobly. All are taxpayers. They worked long, hard hours. They labored without question and with great loyalty to the company. They could devote themselves to the company because they felt secure that as they worked they were earning retirement benefits which would allow them to live, not a luxurious life after retirement, but a life in which they could rest easy, with little financial worry. What has resulted instead is fear, confusion, broken families, and more tragically, attempted and successful suicide.

Mr. John Lipka was a resident of my 17th District, an LTV retiree with 37 years at Truscon (a subsidiary of Republic Steel) and Youngstown Sheet & Tube. Mr. Lipka was a man who was described as "full of life, always whistling." Mr. Lipka's monthly income was $622/month after taxes. When LTV terminated retiree medical insurance the Lipka's found that alternative insurance would cost $572 for three months. With only $800 in savings, the Lipka's knew they could not afford alternative coverage. As described by his wife, Charlotte, even after the medical benefits were restored, Mr. Lipka was afraid they would be taken away again. Mr. Lipka lost weight at a radid pace. He couldn't sleep and developed a phobia that household appliances would break and cost money to be replaced. According to his family, he constantly worried about money -- about how to make ends meet. Most of all, he worried about what would happen after May 15th; would his medical insurance be taken away again? Unfortunately, Mr. Lipka will never know the outcome of this situation. On February 19, 1987, Mr. Lipka put a gun to his head and killed himself. Why? He was afraid of the unkown. He was afraid of the uncertainty regarding his medical benefits and of the financial burden he would face if benefits were terminated.

Is this what our retirees, America's senior citizens, have to look forward to? After a lifetime of hard work, should they be forced to spend their "golden years" worrying about whether or not their life and health insurance needs will be taken care of? Mr. Lipka's death is an extreme tragedy directly resulting from the LTV bankruptcy. And there are other tragedies: retirees with costly medical bills who will not be able to afford alternative insurance cost if benefits are terminated. The LTV Corporation has put the lives of its retirees in jeopardy by not living up to its contractual agreement.

The bill before the committee today, S.548, is just the legislation we need to help these retirees escape the dire situation they now face. Besides revising current Chapter 11 procedural rules, this bill will protect retirees much-needed benefits by preventing the suspension of benefits at the time of bankruptcy. More importantly, it would allow retirees to continue to receive benefits as the company reorganizes and comes out of bankruptcy. S. 548 would ensure the fair and equitable treatment of retirees by clarifying the intent of section 1113 of the bankruptcy code by requiring that a company cannot renege on contractual obligations to their retirees. This legislation would apply to all retirees -- both union and non-union -- covered by employer-employee health care plans.

Most of you are familiar with "Solidarity USA", an LTV retiree organization based in my Congressional District. I hold great respect and admiration for this organization. For the past eight months "Solidarity USA" has made an undying effort to bring the plight of the LTV retirees to the public eye. They have been successful. Now it is time for Congress to act. We have before us the means to clarify a policy which currently allows the bankruptcy code to be used as a weapon to take away the health benefits of our nation's retirees. Our nation's elderly are looking to Congress for a solution. Our inaction on this issue will set a dangerous precedent for other companies to follow. Time is of the essence and I urge the Committee to act favorably, and in an expeditious manner, on the legislative initiative before us today. If not, the health and welfare of our nation's retirees, as well as every working man and woman in America, will be in jeopardy. For some, as we have seen, it could mean the difference between life and death.

Mr. Chairman, Members of the Subcommittee, I would like to thank you for this opportunity to express my support of "The Retiree Benefits Security Act of 1987". At this time, I would be pleased to answer any questions that you may have.

## QUESTIONS AND ANSWERS

Q I AM CONCERNED ABOUT THE FUTURE CONSEQUENCES OF CREATING A SPECIAL EXEMPTION FOR RETIREES FROM THE CHAPTER 11 PROVISIONS OF THE BANKRUPTCY CODE. IS YOUR MAJOR INTEREST PROTECTING THE BENEFITS OF RETIREES OR AMENDING THE BANKRUPTCY CODE? IF YOU ARE INTERESTED IN PROTECTION THE BENEFITS OF RETIREES, DO YOU AGREE THAT WE MIGHT CONSIDER WAYS OF PROTECTING THEM WITHOUT RESORTING TO AMENDING THE CODE?

A My concerns over this issue are two-fold. First and foremost, I am certainly concerned over retirees receiving the benefits for which they worked an entire lifetime. With over 11,000 LTV retirees residing in my Congressional District, I have seen first-hand the adverse effects of the LTV bankruptcy. As my colleagues and I testified, it is essential that the policy regarding benefits in the event of bankruptcy be clarified; if not, the future security of every working man and woman remains in jeopardy. I would very much like to see law enacted that would protect retiree benefits, either within or outside of the bankruptcy code.

Regardless of whether or not the bankruptcy code will be amended to protect retiree benefits, I feel that it must be amended in order to properly address my second concern. That is, I feel the code must be amended in some fashion so that business may not use the bankruptcy code as a means of escaping their responsibilities to their employees. Companies facing financial difficulties due to economic conditions certainly should turn to bankruptcy in order to reorganize to get the company back on its feet. However, I feel the code must be reviewed and amended to prevent companies from declaring bankruptcy as a means of reneging on promises made to employees and retirees. If there should be inaction on this important issue, I fear that we will find more and more companies abusing Chapter 11 as a means to escape their liabilities rather than using Chapter 11 as a legitimate means of reorganization.

Q I AM ALSO CONCERNED THAT THE FUNDAMENTAL PRECEPT OF THE BANKRUPTCY CODE, NAMELY THAT ALL PARTIES ARE TREATED FAIRLY AND EQUITABLE, IS PRESERVED. WHAT SAFEGUARDS DO YOU BELIEVE ARE PRESENT IN THIS BILL TO INSURE THAT ALL UNSECURED CREDITORS ARE TREATED IN A FAIR AND EQUITABLE MANNER IN A CHAPTER 11 PROCEEDING?

A As stated in my testimony, I feel S.548 is a step in the right direction in the effort to adequately protect retiree benefits in the event of bankruptcy. I feel this bill treats parties more fairly than present law, and am especially pleased that the bill gives priority to retiree benefits by placing these individuals in the category where they are treated as an administrative expense. It is my strong hope that this measure will be brought before the Senate and passed in the near future.

I would like to repeat that I am in strong support of S.548. However, as stated in my testimony, I am also in support of a measure which would seek to protect retiree benefits, without modification. S.548 currently contains a provision which would allow for the modificaiton of reitree benefits. I seriously question the modification of retiree beneifts; these retirees worked their entire lifetime for the good of the company, and I strongly feel they should spend their retirement years without worrying about whether or not next month's benefits will cover any illness that the retiree may incur. In my Congressional District retirees are afraid because of the UNCERTAINTY surrounding their benefits. This uncertainty has let to depression and tragic death.

Policy regarding retiree benefits and bankruptcy must be clarified. S.548 would most certainly create policy which is more fair and equitable than present law. However, I also feel that a "no modification" provision regarding retiree benefits would improve and strengthen this measure.

Senator **Heflin**. Senator Metzenbaum, do you have any questions?

Senator **Metzenbaum**. No. I just want to thank Congressman Regula and Congressman Jimmy Traficant for their support of our legislation and for excellent statements. Congressman Traficant has been truly a leader in this whole effort, and we have worked together very well and are going to continue to work together. I appreciate his support. It is meaningful.

Senator **Heflin**. Our next witness is Mr. Lynn Williams, president of the United Steelworkers International of America. Mr. Williams, we are delighted to have you.

Mr. Williams, would you like to introduce the other people?

### STATEMENT OF LYNN WILLIAMS, PRESIDENT, UNITED STEELWORKERS OF AMERICA, ACCOMPANIED BY BRUCE SIMON, BANKRUPTCY COUNSEL; JACK SHEEHAN, HEAD OF LEGISLATIVE DEPARTMENT; AND PAUL WHITEHEAD, COUNSEL, LEGAL DEPARTMENT, PITTSBURGH, PA

Mr. **Williams**. Yes. Thank you very much, Mr. Chairman, for the opportunity to be here. I would like to introduce on my right Bruce Simon, our bankruptcy counsel; on my immediate left Jack Sheehan—who really needs no introduction in these rooms—the head of our legislative department and one of my assistants; and to his left Paul Whitehead, one of our counsel from our legal department in our headquarters in Pittsburgh.

I appreciate the opportunity to present testimony here to you, Mr. Chairman. I appreciate your initiative in having the hearing and appreciate very much Senator Metzenbaum's initiative in dealing with this problem in the legislation which he has proposed.

I will attempt to live within the 5-minute rule, sir, and therefore present some parts of my written testimony, all of which I am sure will go in the record.

Senator **Heflin**. Without objection, your full statement will go in the record.

Mr. **Williams**. Thank you.

This subcommittee is well aware that a wave of bankruptcies, plant shutdowns and mass layoffs is sweeping our Nation's steel industry. While all of basic industry is suffering, no sector has been harder hit than steel. The human suffering is already devastating and it increases by the day.

It is tragic that, despite all of our efforts, we meet today before the Senate subcommittee having jurisdiction over our bankruptcy laws. Steel bankruptcies raise vital concerns for those older Americans who labored for their lifetimes in steel mills to earn the right to receive the basic necessities of their old age. On the day-to-day level, our retirees are concerned about keeping food on their table. On matters of public policy, their concerns focus on our laws affecting trade, pension benefits, pension funding, insurance benefits, mergers and takeovers, and bankruptcy.

Are the reorganization laws fair to retirees? To put it plainly, the issue before us today is whether our reorganization laws give our Nation's retirees a fair shake. I am absolutely certain that if you take a good look at this question, you will conclude that major reform of our bankruptcy laws is urgently needed.

For proof of this point, one need only look to the LTV Steel bankruptcy case. Last July, with the filing of a single document called a chapter 11 petition, LTV Steel cut off all health and life insurance for the tens of thousands of retirees who had given their lives to the company. At the same time, LTV Steel wrote each of the retirees a letter saying that the reorganization laws not only permitted the cutoff of their benefits, but required it. It made this assertion without any regard to the company's ability to afford the benefits.

I understand your subcommittee will hear firsthand from several victims of this action later today. I shall not belabor the record with examples of the hundreds and thousands of heartbreaks, shocks and nightmares caused by this action. Senator Metzenbaum has documented some of these cases by chairing special hearings of this committee in Cleveland last July.

One thing is certain, however. There are few things in a retiree's life so vital as health care. Every retiree lives in fear of being financially wiped out by a long and lingering illness. And for the LTV Steel retiree, the cut-off of their insurance was especially painful for several reasons.

Many LTV retirees are in retirement today because of special company inducements. In order to streamline its work force, LTV Steel offered early pensions and insurance as a retirement incentive to older workers. By accepting these offers, the pensioners helped to make the company more competitive.

Imagine, then, the shock and anger of the LTV Steel retiree who went to his mailbox last July only to learn that one of retirement inducements—his health and life insurance—has been stopped.

It is no wonder, then, that LTV Steel retirees demanded to know how our bankruptcy laws could sanction the cutoff of their benefits. As this subcommittee knows, Congress passed section 1113 of the bankruptcy code in 1984 to prohibit reorganizing companies from unilaterally modifying collectively bargained benefits. Instead, if a company seeks to modify these benefits, it must follow detailed requirements: first, for attempting to negotiate the change; and failing that, for persuading a court that the modifications are necessary to reorganization, fair to all creditors, and consistent with a balancing of the equities.

When Congress adopted these rules in 1984, it applied them to any collectively bargained benefits. Nevertheless, LTV Steel attempted to fabricate an exception to this rule that left retirees completely out in the cold. It was, quite simply, an abuse of our reorganization laws.

In response to the cutoff, I asked steelworkers at the company's Indiana Harbor plant to strike in support of full restoration of the retiree insurance.

After the work stoppage, thousands of pensioners asked Congress to examine how our reorganization laws affect retirees. In the final days of the 99th Congress, as you are all aware, you enacted temporary legislation requiring chapter 11 companies to pay retiree insurance benefits until May 15 of this year. By enacting this stopgap measure, you gave the entire Congress time to study this problem in detail. And so we are here today.

The most critical weakness of our reorganization law is its misconception that a retiree is just like any other unsecured creditor of a company. And based on this error, our current law permits a company to deprive a retiree or a widow of an entire lifetime of insurance protection and treat the loss no differently than the loss of any other creditor. The result is that retirees can receive as little as 5 cents or 10 cents on the dollar for their injury.

Let us examine, for a moment, the typical unsecured creditor in a chapter 11 proceeding. In most cases, the run-of-the-mill creditor is a corporation, often a bank, a utility, an insurance company, or a supplier of goods or services. The typical creditor holds claims, not for something so vital as medical care, but for loans or electrical power or goods supplied or services. These creditors usually do business with a large number of companies so that if one of their customers defaults, the loss affects only a portion of their revenue. And just as importantly, the typical unsecured creditor can protect itself from bad debts in a number of ways.

Now, consider for a moment the average retiree and his or her spouse. Since they are owed health and life insurance by the company, they are, to be sure, creditors of the company. But they could not be more different from the typical unsecured creditor.

At the risk of stating the obvious, the retiree and the retiree's spouse are not a corporation. They cannot absorb the loss of their medical care or life insurance coverage by making an adjustment to a balance sheet or reducing a quarterly dividend to stockholders. They cannot pass their loss on to customers. They cannot spread their risk by charging higher prices across the board. They are, as everyone knows, just two people living on a small and fixed income. The company is their only source of private health insurance.

The retiree, unlike the typical creditor, looks to the company, not for the price of a ton of coal or a kilowatt of power, but for something so basic and life-giving as decent medical care. If the retiree loses so vital a benefit, the effect is an immediate threat to his personal health and well-being. Unlike other individual creditors—employees, for example—retirees cannot go out and find new jobs. Their only refuge is in whatever nest egg they may have, and when that is gone, they may be forced to look to public welfare payments.

Now, I ask you, what other class of creditors of a reorganizing company is in this position? What other class of creditors is just hanging out there in a completely dependent and vulnerable position? What other class of creditors depends on the company for the very basics of life and health? What other class of creditors can say, if it takes a loss in a reorganization, that its members will be unable to pay for prescriptions or even afford to bury a spouse with dignity?

I think the evidence is simply overwhelming that retirees are truly unique among all creditors in a chapter 11 proceeding both in the nature of their claims and in the devastating impact of their losses. Since the retiree does not begin on an equal par with other creditors, so-called equal treatment with other unsecured creditors is really not equal treatment at all. Instead, it will leave the retiree right where he began—behind the other creditors in his standard of living, financial wherewithal and peace of mind.

Outside of our reorganization laws, Congress has recognized the vulnerability of retirees and has gone to some length to protect their expectations. But not so with our reorganization laws. Something is wrong in this country when companies are allowed to reorganize on the backs of the very people who built the company. It is time for Congress to put some common sense and social conscience into our reorganization laws.

Let me emphasize that this is not just an LTV Steel problem, nor is it just a steel industry problem. Companies in every sector of our economy are embarking on major restructurings by inducing thousands and thousands of their older employees to retire. Those companies include not just the giants like ITT, IBM, Xerox, and the oil companies, but hundreds of medium and smaller corporations. If their restructurings prove ineffective and any of these companies are forced to seek the protection of chapter 11, how will their retirees have any security in their benefit programs?

I cannot emphasize strongly enough the depth of feeling that retirees have on this subject, and it is entirely legitimate. They perceive our Nation's system of justice as unfair and even vicious when it allows a bankruptcy court to preside over the wiping out of fixed-income households. They are demanding to know whether there is any integrity or credibility to the private health insurance system in our country.

This problem cries out for solutions. And in the search for a cure, the Steelworkers Union holds to three fundamental beliefs. First, retiree expectations are worthy of the fullest protection of our Federal laws. Congress must make it the public policy of this country that retiree benefits—once promised and earned from a lifetime of labor—be paid, be paid in full, and be paid without forcing retirees to worry, fret, sue, picket, or march on Washington.

Second, the reform of our bankruptcy law is an essential step toward full guarantees of retiree expectations under Federal law, but it is only a first step. Retiree insurance benefits are unfunded and unguaranteed. Under any conceivable amendment to our reorganization laws, companies will always be capable of liquidating or being liquidated and retirees will lose.

That leads to our third principle. The full protection of retiree insurance necessarily demands nonbankruptcy legislation as well. We must take a two-track approach.

On the nonbankruptcy side, we are pushing proposals for extensions of Medicare, the prefunding of retiree insurance benefits, and the creation of a PBGC-like agency for the backing up of retiree insurance commitments. We are working toward the development of a national health insurance plan as well. Only these systems can provide complete security. But none of them detracts from the immediate need to reform our reorganization laws, and I mean immediate. On May 15, the stopgap legislation expires. If we are unable to win meaningful reform of our laws before May 15, we ask Congress to extend that deadline.

Let us turn now to the provisions of S. 548 and its companion bill in the House, H.R. 1186. We enthusiastically support this bill. With the other Federal law changes I have spoken of, it achieves the important reforms that are needed in our reorganization laws.

First, S. 548 reaffirms Congress' command that the benefits of retired workers, like those of active employees, cannot be unilaterally cut with the filing of a bankruptcy petition. S. 548 directs chapter 11 companies to pay retirees their full level of health, life, and other insurance benefits until and unless a modification in those benefits either is negotiated between the company and the representative of the retirees, or if negotiations fail, is approved by a bankruptcy court.

Second, S. 548 permits a court to approve only those modifications in retiree insurance benefits that are necessary, fair, and equitable. More specifically, it limits modifications in retiree benefits to those that are necessary to permit the reorganization of the debtor, fair to all creditors, and consistent with a balancing of the equities.

Third, the legislation makes clear that any required payment of retiree insurance during a reorganization has the status of an administrative expense. This puts retiree benefits during the reorganization on the same priority levels as the wages and benefits of active employees.

Fourth, S. 548 gives retirees a greater voice in the formulation of a reorganization plan. Recognizing the unique status of retiree creditors and their claims, the proposed legislation places the insurance claims of retiree creditors in a separate class for voting on a reorganization plan.

Fifth, S. 548 modifies the procedures of title 11 for final approval of a reorganization plan. In particular, it addresses the situation where the class of retiree insurance claimants votes against a proposed reorganization plan. Thereafter, a court may approve the plan over the objection of retirees provided the court makes a critical finding. That is a determination that the plan accords retirees the value representing the minimum modifications in retiree benefits consistent with the ability of the company to provide benefits in the post-bankruptcy period.

Sixth, the proposed legislation applies to union and salaried (nonunion) retirees.

In closing, let me respond briefly to the major argument that has been raised by the bankruptcy bar against this legislation. They argue that S. 548 will make reorganizations impossible and cause liquidations. The argument is simply wrong. It does, however, have a familiar ring to it because it is the same opposition that was advanced against section 1113 before its adoption in 1984. Those dire predictions from 1984 did not come true, nor will they occur under this proposed legislation. That is because S. 548 adopts as one of its standards what is necessary to permit reorganization. I ask that you keep this point in mind as the debate unfolds.

Thank you for your attention. I pledge to work with all of you both within and outside the bankruptcy code to resolve a major problem facing the retirees of this country. [Applause.]

[Submissions of Mr. Williams follow:]

## Statement of

Lynn Williams, President
UNITED STEELWORKERS OF AMERICA

I am particularly honored to speak today on behalf of retired Steelworkers across this country. Some 1,600 of those retirees and their spouses rally with me in Washington today to express our support for a reform of our nation's bankruptcy laws. I commend this Subcommittee for holding these timely hearings and thank you for the opportunity to present the views of the Steelworkers Union.

This Subcommittee is well aware that a wave of bankruptcies, plant shutdowns, and mass layoffs is sweeping our nation's steel industry. While all of basic industry is suffering, no sector has been hit harder than steel. The human suffering is already devastating and it increases by the day.

Throughout this period, every Steelworker in every steel mill in this country has acccepted sacrifices in recognition of the problems facing the steel industry. At the same time, our Union has repeatedly urged the Administration to go to the source of the steel industry's problems by adopting sensible industrial and trade policies. Time and again, we have asked the Administration to practice some preventive medicine -- to get ahead of the problems in basic industry -- by amending our laws affecting trade, taxation, reinvestment, the improvement of our infrastructure, retraining, etc.

### The Wave of Bankruptcies

It is tragic that -- despite all of our efforts -- we meet today before the Senate Subcommittee having jurisdiction over our bankruptcy laws. Let me list for you just a few of the steel companies that have been forced to reorganize under our bankruptcy laws: LTV Steel, (a company that embodies what once was Youngstown Sheet and Tube, Jones and Laughlin Steel and Republic Steel), Wheeling-Pittsburgh Steel, Kaiser Steel of Fontana, California, McLouth Steel of Detroit, Continental Steel of Indiana, Mesta Machine of Pittsburgh, Eastern Stainless Steel of Baltimore, Phoenix Steel of Philadelphia and Claymont, Delaware, Guterl Steel and Roblin Steel of the Buffalo area, and the list just goes on and on with medium-and smaller-size companies.

These bankruptcies raise vital concerns for those older Americans who labored for their lifetimes in steel mills to earn the right to receive the basic necessities of their old age. On the day to day level, our retirees are concerned about keeping food on their tables. On matters of public policy, their concerns focus on our laws affecting trade, pension benefits, pension funding, insurance benefits, mergers and takovers, and bankruptcy.

I recognize that Congress has specialized committees to deal with each of these problems in detail. And I realize too that today's hearing focuses on our bankruptcy laws, particularly on how our reorganization laws treat retiree insurance benefits. Before turning to that topic, let me emphasize that insurance problems are by no means the only crisis facing steel retirees today.

## The Pension Crisis in Steel

Just last week, our Union came to Washington to call for crucial improvements -- not only in our bankruptcy laws --but in our federal pension law. In the wake of the termination of the LTV Steel pension plans, we have asked Congress to extend the protections of the Pension Benefit Guaranty Corporation (PBGC) to a monthly pension benefit in the steel industry known as the "$400 supplement" for early pensioners. Many of the 1,600 retirees with me today have been devastated by the loss of their $400 monthly pension supplements, payments that in some cases amounts to half of a pensioner's income or even more. Our Union is litigating, lobbying and negotiating to restore these payments. As we discuss retiree insurance problems today, please bear in mind that for thousands of LTV Steel retirees, the loss of these and other pension benefits combined with the possible loss of retiree insurance threatens nothing other than personal and family disaster.

### Are the Reorganization Laws Fair to Retirees?

To put it plainly, the issue before us today is whether our reorganization laws give our nation's retirees a fair shake. I am absolutely certain that if you take a good look at this question, you will conclude that major reform of our bankruptcy laws is urgently needed.

### The LTV Steel Example

For proof of this point, one need only look to the LTV Steel bankruptcy case. Last July, with the filing of a single document called a Chapter 11 petition, LTV Steel cut off all health and life insurance for the tens of thousands of retirees who had given their lives to the company. At the same time, LTV Steel wrote each of the retirees a letter saying that the reorganization laws not only permitted the cutoff of their benefits, but required it. And it made this assertion without any regard to the company's ability to afford the benefits.

I understand your Subcommittee will hear first hand from several victims of this action later today. I shall not belabor the record with examples of the hundreds and thousands of heartbreaks, shocks and nightmares caused by this action. Senator Metzenbaum has documented some of these cases by chairing special hearings of this Committee in Cleveland last July.

One thing is certain, however. There are few things in a retiree's life so vital as health care. Every retiree lives in fear of being financially wiped out by a long and lingering illness. And for the LTV Steel retiree, the cutoff of their insurance was especially painful for two reasons.

## The "Bait and Switch"

Many LTV Steel retirees are in retirement today because of special company inducements. In order to streamline its work force, LTV Steel offered early pensions and insurance as a retirement incentive to older workers. By accepting these offers, the pensioners helped to make the company more competitive.

Imagine then the shock and anger of the LTV Steel retiree who went to his mailbox last July only to learn that one of retirement inducements -- his health and life insurance --had been stopped.

## The Lack of Medicare for Many Retirees

Second, many LTV Steel retirees are under the age of 65 and therefore do not qualify for Medicare. For them, their company-paid health insurance is their only access to medical care. Obviously, retirees over 65 need private insurance against major gaps in Medicare coverage. Their "Medicare wrap-around" insurance spares them from the expenses of doctor visits, prescription costs, and a host of other expenses.

But for a retiree under 65 -- as tens of thousands of LTV Steel retirees are -- company paid health insurance is all they have. Let me emphasize that. For early pensioners, company-paid health insurance is their only protection from the devastating cost of totally uninsured medical bills.

## Corporate Contempt for the Law

It is no wonder then that LTV Steel retirees demanded to know how our bankruptcy laws could sanction the cutoff of their benefits. As this Subcommittee knows, Congress passed

Section 1113 of the bankruptcy code in 1984 to prohibit reorganizing companies from unilaterally modifying collectively bargained benefits. Instead, if a company seeks to modify those benefits, it must follow detailed requirements, first, for attempting to negotiate the change and, failing that, for persuading a court that the modifications are necessary to reorganization, fair to all creditors, and consistent with a balancing of the equities.

When Congress adopted these rules in 1984, it applied them to any collectively bargained benefits. Nevertheless, LTV Steel attempted to fabricate an exception to this rule that left retirees completely out in the cold. It was, quite simply, an abuse of our reorganization laws.

## The LTV Strike

In response to the cutoff, I asked Steelworkers at the company's Indiana Harbor plant to strike in support of full restoration of the retiree insurance. The strike was the right thing to do, it came at the right time, and it could make a real difference in righting a corporate wrong. Within a week, the benefits were restored for a six-month period.

I am particularly proud of the Indiana Harbor Steelworkers and those at other locations as well who were willing to sacrifice their paychecks. I would like all of America to know that unionized employees will fight for the welfare of others, especially those less able to defend themselves.

## The Aftermath

After the work stoppage, thousands of pensioners asked Congress to examine how our reorganization laws affect retirees. In the final days of the 99th Congress, as you are all aware, you enacted temporary legislation requiring Chapter 11 companies to pay retiree insurance benefits until May 15 of this year. By enacting this stopgap measure, you gave the entire Congress time to study this problem in detail. And so we are here today.

## The Defect in our Bankruptcy Law

The most critical weakness of our reorganization law is its misconception that a retiree is just like any other unsecured creditor of a company. And based on this error, our current law permits a company to deprive a retiree or a widow of an entire lifetime of insurance protection and treat the loss no differently than the loss of any other creditor. The result is that retirees can receive as little as 5¢ or 10¢ on the dollar for their injury. In some courts, the retiree who has lost a lifetime of coverage is permitted to pursue a claim for only one year's damages.

## The Typical Creditor in Chapter 11

Let's examine for a moment the typical unsecured creditor in a Chapter 11 proceeding. In most cases, the run-of-the-mill creditor is a corporation, often a bank, a utility, an insurance company, or a supplier of goods or services. The typical creditor holds claims --not for something so vital as medical care --but for loans, or electrical power, or goods supplied, or services. These creditors usually do business with a large number of companies so that if one of their customers defaults, the loss affects only a portion of their revenues.

And just as importantly, the typical unsecured creditor can protect itself from bad debts in a number of ways. For example, if a reorganizing company defaults on an obligation, the typical creditor corporation can seek new business to make up for the loss. Indeed, by accepting a loss on its claim, the typical creditor may be able to save a customer and the chance of future profits from that customer. In any event, the typical Chapter 11 creditor can increase the price it charges to all customers and thereby spread the risk of any one customer defaulting in whole or part. And if the worst happens, and a debt goes completely sour, the usual creditor has been able to take a tax deduction for a bad debt.

### The Retiree Creditor -- A Different Story

Now consider for a moment the average retiree and his or her spouse. Since they are owed health and life insurance by the company, they are, to be sure, creditors of the company. But they could not be more different from the typical unsecured creditor.

At the risk of stating the obvious, the retiree and the retiree's spouse are not a corporation. They cannot absorb the loss of their medical care or life insurance coverage by making an adjustment to a balance sheet or reducing a quarterly dividend to stockholders. They cannot pass their loss on to customers. They cannot spread their risk by charging higher prices across the board. They are, as everyone knows, just two people living on a small and fixed income. And the company is their only source of private health insurance.

The retiree, unlike the typical creditor, looks to the company -- not for the price of a ton of coal or a kilowatt of power -- but for something so basic and life-giving as decent medical care. If the retiree loses so vital a benefit, the effect is an immediate threat to his personal health and well-being. Unlike other individual creditors -- employees for example -- retirees cannot go out and find new jobs. Their only refuge is in whatever nest egg they may have, and when that is gone, they may be forced to look to public welfare payments.

Now I ask you, what other class of creditors of a reorganizing company is in this position? What other class of creditors is just hanging out there in a completely dependent and vulnerable position? What other class of creditors depends on the company for the very basics of life and health? What other class of creditors can say, if it takes a loss in a reorganization, that its members will be unable to pay for prescriptions or even afford to bury a spouse with dignity?

**The Case for Reform**

I think the evidence is just overwhelming that retirees are truly unique among all creditors in a Chapter 11 proceeding both in the nature of their claims and in the devastating impact of their losses. Since the retiree does not begin on an equal par with other creditors, so-called "equal treatment" with other unsecured creditors is really not equal treatment at all. Instead, it will leave the retiree right where he began--behind the other creditors in his standard of living, financial wherewithal and peace of mind.

Outside of our reorganization laws, Congress has recognized the vulnerability of retirees and has gone to some length to protect their expectations. But not so with our reorganization laws. Something is wrong in this country when companies are allowed to reorganize on the backs of the very people who built the company. It is time for Congress to put some common sense and social conscience into our reorganization laws.

Let me emphasize that this is not just an LTV Steel problem, nor is it just a steel industry problem. Companies in every sector of our economy are embarking on major restructurings by inducing thousands and thousands of their older employees to retire. Those companies include not just the giants like ITT, IBM, Xerox, and the oil companies, but hundreds of medium and smaller corporations. If their restructurings prove ineffective and any of these companies are forced to seek the protection of Chapter 11, how will their retirees have any security in their benefit programs?

I cannot emphasize strongly enough the depth of feeling that retirees have on this subject and it is entirely legitimate. They perceive our nation's system of justice as unfair and even vicious when it allows a bankruptcy court to preside over the wiping out of fixed-income households. They are demanding to know whether there is any integrity or credibility to the private health insurance system in our country.

## The Fundamentals of a Solution

This problem cries out for solutions. And in the search for a cure, the Steelworkers Union holds to three fundamental beliefs. First, retiree expectations are worthy of the fullest protection of our federal laws. Congress must make it the public policy of this country that retiree benefits -- once promised and earned from a lifetime of labor -- be paid, be paid in full, and be paid without forcing retirees to worry, fret, sue, picket, or march on Washington. Retiree benefits are deferred wages and their non-payment amounts to a bilking of honest working people.

Second, the reform of our bankruptcy law is an essential step toward full guarantees of retiree expectations under federal law, but it is only a first step. Retiree insurance benefits are unfunded and unguaranteed, Under any conceivable amendment to our reorganization laws, companies will always be capable of liquidating or being liquidated and retirees will lose. We live in a competitive economy that sees companies die every day.

And that leads to our third principle. The full protection of retiree insurance necessarily demands non-bankruptcy legislation as well. We must take a two-track approach.

On the non-bankruptcy side, we are pushing proposals for extensions of Medicare, the pre-funding of retiree insurance benefits, and the creation of a PBGC-like agency for the backing up of retiree insurance commitments. And we are working toward the development of national health insurance as well. Only these systems can provide complete security. But none of them detracts from the immediate need to reform our reorganization laws, and I mean immediate. On May 15, the stopgap legislation expires. If we are unable to win meaningful reform of our laws before May 15, we ask Congress to extend that deadline.

### Senate Bill No. S. 548

Let's turn now to the provisions of S. 548 and its companion bill in the House, H.R. 1186. We enthusiastically support this bill. With the other federal law changes I have spoken of, it achieves the important reforms that are needed in our reorganization laws.

First, S. 548 reaffirms Congress's command that the benefits of retired workers, like those of active employees, cannot be unilaterally cut with the filing of a bankruptcy petition. S. 548 directs Chapter 11 companies to pay retirees their full level of health, life, and other insurance benefits until and unless a modification in those benefits either is negotiated between the company and the representative of the retirees, or if negotiations fail, is approved by a bankruptcy court.

Second, S. 548 permits a court to approve only those modifications in retiree insurance benefits that are necessary, fair, and equitable. More specifically, it limits modifications in retiree benefits to those that are necessary to permit the reorganization of the debtor, fair to all creditors, and consistent with a balancing of the equities.

I might note that these are significant and meaningful standards. I would point to the Third Circuit's opinion in the Wheeling-Pittsburgh case as an example. There, the court correctly concluded that cuts in collectively bargained benefits are "necessary to permit reorganization" when they are needed to avoid a liquidation. Thus, retiree benefits can be modified under S. 548 only when necessary to avoid liquidation. Obviously, all creditors -- incluing retirees -- have a substantial interest in avoiding liquidation.

Third, the proposed legislation provides that, if a modification is approved, the resulting coverage during the reorganization may not fall below what is neccessary, fair, and equitable.

Fourth, the legislation makes clear that any required payment of retiree insurance during a reorganization has the status of an administrative expense. This puts retiree benefits during the reorganization on the same priority levels as the wages and benefits of active employees.

Fifth, S. 548 gives retirees a greater voice in the formulation of a reorganization plan. Recognizing the unique status of retiree creditors and their claims, the proposed legislation places the insurance claims of retiree creditors in a separate class for voting on a reorganization plan.

Sixth, S. 548 modifies the procedures of Title 11 for final approval of a reorganization plan. In particular, it addresses the situation where the class of retiree insurance claimants votes against a proposed reorganization plan. Thereafter, a court may approve the plan over the objection of retirees provided the court makes a critical finding. That is a determination that the plan accords retirees the value representing the minimum modifications in retiree benefits consistent with the ability of the company to provide benefits in the post-bankruptcy period.

Seventh, the proposed legislation applies to union and salaried (non-union) retirees. For the salaried group, the court must appoint a committee of retiree representatives.

For union retirees, the bill authorizes unions to serve as their representative. Our Union believes that it is essential that union retirees be represented by the organization that negotiated these benefits in the first place and the entity that can, if necessary, engage in economic action against their unjustified reduction. But in light of conflict of interest concerns discussed in the Century Brass decision, the legislation also allows unions to decline to serve as retiree representatives. In that event, the court must appoint --as in the case of salaried retirees --a committee of representatives for union retirees.

Finally, the proposed legislation exempts retiree claims from the one-year limitation-on-damages rule I spoke of earlier. Under Section 502(b)(7) of the Bankruptcy Code, certain claims arising from the termination of an employment contract are limited to one year's duration. The purpose of the rule is to prevent highly paid executives from asserting large claims for the breach of lucrative "golden parachute" contracts. However, some courts have applied this rule to limit retiree claims under collective bargaining agreements to a fraction of their value. The proposed legislation removes this inequity for both union and non-union retirees.

## Conclusion

In closing, let me respond briefly to the major argument that has been raised by the bankruptcy bar against this legislation. They argue that S. 548 will make reorganizations impossible and cause liquidations.
The argument is simply wrong. It does, however, have a familiar ring to it because it is the same opposition that was advanced against Section 1113 before its adoption in 1984. Those dire predictions from 1984 did not come true, nor will they occur under this proposed legislation. That's

because S. 548 adopts as one of its standards what is necessary to permit reorganization. I ask that you keep this point in mind as the debate unfolds.

Thank you for your attention. I pledge to work with all of you both within and outside the bankruptcy code to resolve a major problem facing the retirees of this country.

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Lynn R. Williams
International President

SENATOR HEFLIN
[illegible] PM 2:23

June 8, 1987

The Honorable Howell Heflin
United States Senate
Senate Hart Office Building
2nd Street & Constitution Avenue, NE
Washington, DC 20510

Dear Senator Heflin:

Thank you for the opportunity to answer the three questions (copy attached) submitted as a follow-up to my April 1 testimony before your Subcommittee. I shall first address your questions concerning possible conflicts of interest between retirees and active employees.

For the reasons given below, we in the Steelworkers Union believe that the reorganization laws should regard a labor organization in proceedings under Section 1113 of the Bankruptcy Code as the presumptively appropriate representative of those who retired from the union's bargaining unit.

In most collective bargaining situations, there is a substantial harmony of interest between active and retired employees. Often, the active workers and the retirees are close family relatives of each other. For this reason alone, employees refrain from even considering the imposition of undue sacrifices on retirees.

Active employees also have a self-interest in avoiding unfair treatment of retirees. Such treatment sets a dangerous precedent for the active employee's own retirement years. Most workers look forward to retirement security. It seriously disrupts the employees' peace of mind about their own retirement years to see retirees unfairly treated. I believe this is why Steelworkers at the LTV Indiana Harbor plant so willingly went on strike last July to force LTV Steel to reverse the cutoff of retiree health insurance.

For their part, retirees customarily understand that some sacrifice on their part may be necessary to help save the company that pays their retiree benefits.

I do not mean to suggest that there can never be a conflict of interest between active employees and retirees. But there is significant congruence of interests, and to the extent there is conflict or potential conflict, it is not unlike that routinely faced by unions. In collective bargaining, whether inside or outside of bankruptcy, unions must balance the competing claims of skilled workers vs. unskilled, the concerns of employees at one plant vs. another, the demands of older workers vs. younger workers, active vs. laid off, and, to be sure, retired vs. non-retired.

Subsections 1113(h) and (i) are consistent with these realities of collective bargaining. Those subsections permit -- but do not require -- unions to represent retirees. If the union believes it can represent retirees without a disabling conflict of interest, it may do so. If the union perceives a serious conflict of potential conflict, or if it wishes to decline to represent the retirees for some other reason, it may do so. In any event, we believe a bankruptcy court has -- under current bankruptcy law -- the inherent equitable power to step in and redress an actual conflict of interest situation.

There is an important pragmatic point arguing in favor of the approach in Subsections 1113(h) and (i). That is the benefit that redounds to retirees when they are represented by an organization with economic power. Recent experience suggests that the reorganization laws can be used by companies to overreach in the taking of benefits from workers and retirees. Frequently, legal protection does not prevent the overreaching. A critical protection for workers and retirees are the economic weapons available to a union.

This point causes me to question those who would suggest that unions should never represent retirees for supposed conflict of interest problems. Often, the advocates of that position are banks, insurance companies, and other major financial institutions -- entities that frequently support the elimination of retiree benefits in bankruptcy cases. One may ask whether the conflict of interest issue is simply being used as a device to deprive retirees of the protections inherent in the use of the strike weapon.

The answer to the first part of your third question is "yes." S. 548 would amend 1113(f) so as to include pension benefits in the scope of that subsection's protection. This achieves a consistency with the provisions of SEPPAA (the Single Employer Pension Plan Amendment Act), since SEPPAA prevents the Pension Benefit Guaranty Corporation from processing the voluntary termination of a pension when the termination violates a collective bargaining agreement. Thus, for voluntary terminations, 1113(f) would add its voice to SEPPAA by making it clear that a company must seek relief from any contractual obligation to maintain a pension plan before terminating a pension and causing the possible loss of pension benefits. The 1113(f) amendment would clarify our understanding of the current effect of 1113.

With respect to involuntary pension terminations, SEPPAA appears to permit the PBGC to commence an involuntary termination even in the face of a collective bargaining agreement that requires an employer to maintain the plan. To be sure, if the PBGC succeeded in obtaining the involuntary termination, 1113(f) would require the company to continue paying the full level of promised benefits under any still unrejected collective bargaining agreement. This, however, is not a conflict between SEPPAA and the proposed language of 1113(f).

I hope these answers are useful to your Subcommittee and I repeat the Union's pledge to cooperate fully with your Subcommittee in achieving the important reforms represented by S. 548.

Sincerely yours,

Lynn R Williams

LYNN R. WILLIAMS
International President

Enclosure

## QUESTIONS FOR LYNN WILLIAMS

1. New subsections 1113 (h) and (i) of S.548 authorize the labor organization, which is the recognized exclusive bargaining representative to be the authorized representative of retired employees unless the authorized representative elects not to serve. Do you see a conflict with allowing the union to represent both retired employees and active employees?

2. If the union representing the current employees is trying to maintain current wages and the union is also trying to maintain the benefits of retired workers, is there not a conflict by the nature of the interests?

3. S.548 would amend section 1113 (f) by adding the language "including any provision relating to benefits for retired employees." Would this language include pension benefits? Is this not in conflict with legislation passed as a part of the reconciliation bill last year which provided that to terminate pension benefits, a company had to comply with the ERISA laws? Does this not severely impact upon a company's ability to reorganize?

Senator **Heflin**. I believe you have a few members of your union with you.

Mr. **Williams**. There is a great interest in this problem, sir.

Senator **Metzenbaum**. I think those were the bankruptcy lawyers. [Laughter.]

Mr. **Williams**. I applaud your optimism.

Senator **Heflin**. You might like to have a show of hands of the ones from Ohio, the members of the Steelworkers Union that are here. [A show of about 10 hands.]

How about the ones from Alabama? [A show of about 15 hands.]

How about the ones from Pennsylvania?

Mr. **Williams**. We have, Senator, 1,300 retirees in town from all of those fine places you have just mentioned. We could have had an indefinite number. We would have had 1,600 except the weather in Mr. Metzenbaum's city of Cleveland there was so bad that six busloads were not able to come because the bus drivers, well, thought it was unwise and clearly irresponsible to tackle the weather. We have quite a group in town.

Senator **Metzenbaum**. The Lord is on my side in most other areas; maybe on this one he was not.

Mr. **Williams**. Well, nobody has demonstrated a great ability to control the weather, Senator.

Senator **Heflin**. Mr. Williams, how many retirees of the LTV Corporation are under 65? And what special problems do these retirees incur?

Mr. **Williams**. A rough estimate is about 20,000 are under 65 and, therefore, do not have access to Medicare and were left, when they received the company letter, completely without health care services.

Senator **Heflin**. Now, what happens to the benefits of a retiree who retires at age 55 and then seeks employment elsewhere, and as a result of that employment has additional medical or health benefit coverage? Does that in any way affect the coverage provided by the first company?

Mr. **Williams**. That is such an unusual experience that I cannot really respond to that. It is a coordination of benefits in all these circumstances. In other words, it is not permitted, that a person, a retiree in some way could receive double benefits for any illness or anything of that kind. In all these insurance plans between various employers and so on, benefits are coordinated.

But, in truth, the circumstance in the steel towns, let me assure you, in the Aliquippas of this world and the Birminghams in terms of unemployment in the steel industry, is that for most people aged 55 or over, the possibility of securing other employment of any significance, at least—and really other employment at all—is such an unusual experience that that is not the problem.

Senator **Heflin**. Well, generally, you have some sort of provision that insurance companies themselves have in their contracts pertaining to primary coverage and supplemental coverage.

Mr. **Williams**. Exactly.

Senator **Heflin**. The same is true, I suppose, relative to Medicare and any other insurance that is held if you are over 65?

Mr. **Williams**. Yes. There are offsets in all of those arrangements.

Senator HEFLIN. Senator Metzenbaum.

Senator METZENBAUM. I have a couple questions, yes.

President Williams, Wheeling-Pitt Steel is currently in bankruptcy. Did that company ever suspend the retiree health benefits?

Mr. WILLIAMS. No, sir, they did not. The retiree health benefits were maintained, and in the subsequent collective agreement that was negotiated at Wheeling-Pitt, they continued to be maintained.

Senator METZENBAUM. So the contention of LTV that the law mandates termination of retiree health benefits is not correct?

Mr. WILLIAMS. Absolutely wrong. That is why we took the action we did in the union of asking our members at Indiana Harbor to go on strike in support of the retirees. We had a plan in place to extend those stoppages to other critical plants of LTV because we were absolutely certain, in terms of our advice and our own knowledge, that what they alleged the law required them to do was not, in fact, the case.

Senator METZENBAUM. I have heard from union and non-union retirees of Kaiser Steel, which filed for bankruptcy in February of this year, that despite the stopgap measure, Kaiser has terminated benefits for 3,700 retirees.

As a matter of fact, at this point, Mr. Chairman, I ask that a letter from District Director Robert A. Guadiano of the United Steelworkers of America and a letter from Roath and Brega, P.C., be included in the record.

Mr. WILLIAMS. Your information is accurate.

Senator HEFLIN. Without objection, so ordered.

[The following letters were submitted for the record:]

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LOUIS E. GELT
GREGORY C. TEVIS
OF COUNSEL

March 18, 1987

The Honorable Howard Metzenbaum
United States Senate
Washington, D.C. 20510

Re: S. 548

Dear Senator Metzenbaum:

As you probably know, Kaiser Steel Corporation and its subsidiaries filed for Chapter 11 bankruptcy protection on February 11, 1987, in the United States Bankruptcy Court for the District of Colorado. This firm has been retained to represent a subcommittee of the Official Unsecured Creditors' Committee known as the "Retiree Subcommittee." The Retiree Subcommittee is a group of four retirees of Kaiser Steel who will collectively represent the interests of approximately 6,000 or more Kaiser Steel retirees who now find themselves with extremely uncertain medical, sickness or disability benefits as a result of the bankruptcy filing. We will serve as counsel for the Retiree Subcommittee in the Chapter 11 proceedings.

Obviously, my clients take a keen interest in the status of Senate Bill 548. We understand that a hearing is set for Wednesday, April 1, 1987 at 10:00 a.m., before the Judiciary Committee's Subcommittee on Courts and Administrative Practice. We would be happy to attend this hearing, and address such issues as relate to the predicament of the retirees of Kaiser Steel. I can assure you that the tension between the general unsecured creditors, who, in most instances, have dealt with the company since the closing of the steel mill in 1983 and the retirement of my clients, is very real and will no doubt be employed by the debtor and other creditors for various types of leverage in the bankruptcy proceedings. We had been preparing our suggestions for a restructuring of the prior statute, when we received a synopsis of Senate Bill 548, and found that most of the language which we would have suggested has been incorporated in the bill.

However, one area is of particular concern to Kaiser retirees: Kaiser asserts that it terminated its benefit plans prior to the filing of the bankruptcy petition, such that it is not obligated to fund those claims post-petition, nor would those claims arguably fall within the language of S. 548 as it is now drafted. So long as S. 548 retains a provision that it be retroactive, and incorporates also a provision to the effect that a purported termination of benefits within 90 days prior to the filing of a bankruptcy petition (or an involuntary petition) is not effective to place the claims outside the statute, the proposed legislation may be of incalculable benefit to the interests of the retirees of Kaiser Steel.

We would very much like to discuss these issues with either yourself or a member of your staff. We believe that the interests of the retirees of Kaiser Steel, in this new bankruptcy proceeding, would be of interest to the Subcommittee on Courts and Administrative Practice, but would obviously defer to you as to whether testimony at the April 1, 1987 hearing would indeed be valuable. If you could have someone contact me as soon as possible to discuss the Kaiser Steel case, and the impact of the proposed legislation on thousands of Kaiser Steel's retirees who will depend upon the outcome of these bankruptcy proceedings for many of these benefits, I would appreciate it very much.

Sincerely,

Carl a Eklund

Carl A. Eklund

CAE:keg

cc: Ronald Bitonti
Tom Rabone
Robert Pritchett
Travis Case
Lyle Stevenson
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ROBERT R. GUADIANA, *Director*

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The Honorable Howard M. Metzenbaum
**U. S. Senate**
140 Senate Russell Office Building
Washington, D. C. 20510-3502

March 30, 1987

RE: **The Retiree Benefits Security Act of 1987**
**SENATE BILL 548**

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Dear Senator Metzenbaum:

Our Union, as you know, wholeheartedly supports the Retirement Benefits Security Act of 1987, which you introduced in the United States Senate. On April 1, 1987, our International President Lynn R. Williams will be testifying in support of the bill, and some 1,600 retirees of the LTV Steel Company will be traveling to Washington to demonstrate the need for Bankruptcy Code reform to protect their hard-won retiree health and insurance benefits. The importance of the bill to thousands of retirees across the country is amply illustrated by the hardship now confronting the retirees of the Kaiser Steel Corporation whose steel-making facility in Fontana, California closed its doors in 1983.

In February 1987, Kaiser Steel and its subsidiaries filed for protection under Chapter 11 of the Bankruptcy Code. But, less than three (3) weeks before that filing, Kaiser Steel informed almost 3,700 retirees and surviving spouses that it would no longer pay for their health and life insurance coverage.

For these retirees and surviving spouses, the Company's announcement was nothing short of betrayal. In 1984, these individuals agreed to shoulder part of the cost of their health insurance coverage, and Kaiser Steel explicitly acknowledged that it was obligated to provide lifetime insurance to these very retirees and surviving spouses. When Kaiser Steel abruptly cancelled retiree coverage, a lawsuit, seeking an injunction against the breach of the agreement between the Union and Kaiser Steel was filed. Only the filing of the Chapter 11 petition and the protection of the automatic stay prevented the Union from obtaining a restoration of the needed health benefits.

Arizona California Nevada New Mexico

Our Union is taking an active part in the bankruptcy proceeding and has assumed a leadership role on behalf of the retiree creditors. Although Kaiser's financial records are in considerable disarray at present, the accountants for the Creditors' Committee, Coopers and Lybrand, are conducting an examination of them. We intend to use the study to determine how best to enforce the provisions of Public Law 99-500 which you guided into law. Kaiser Steel claims to have insufficient cash to comply with the legislation, though it certainly has assets sufficient to finance compliance. Whatever the results of the accountants' study, our Union will seek to enforce retiree rights in a manner that will maximize their interests in continued employer-paid health and life insurance. We hope to have sufficient accounting information within the next two weeks to make our decision.

But more importantly, and setting aside the complexities and legalisms, the potential for personal and family disaster in this situation is very real. Permit me to briefly describe to you the condition of just seven of the over 3,700 individuals whose interests we seek to protect. The brief summaries that follow are taken from sworn statements obtained from over a thousand of the retirees and widows we represent.

One retiree worked 22 years for Kaiser Steel and receives a monthly pension of only $391.00. He is disabled as a result of an occupational injury and cannot work to supplement his minimal pension income. The costs of prescriptions for heart and lung conditions and medical coverage for him and his spouse threaten his economic survival.

The widow of a Kaiser Steel retiree receives a monthly benefit in the amount of $77.50. Prescriptions for her congestive heart trouble alone cost between $75.00 and $100.00 per month. Even before paying the monthly conversion cost of almost $39.00 for health coverage, her income from the pension plan totally disappears.

Another retiree worked for Kaiser for 23½ years and receives a net pension of $294.00 a month. After paying for his own health coverage, that pension will be reduced to $219.00. He tells us, "I feel that Kaiser should pay for my health benefits, because I worked hard for 23 years for Kaiser and.....they made a promise."

One 27½ year former Kaiser employee now receives a net pension of $735.00. Part of that is a supplement of $400 which will not be guaranteed by the Pension Benefit Guaranty Corporation in the event the Kaiser Pension Plan for hourly employees is terminated. The conversion cost for medical benefits would reduce his current pension to $485.00 per month, and this is not enough for the retiree and his spouse to get by on.

The surviving spouse of a 25-year Kaiser employee receives only $90.00 per month in pension benefits. The $76.00 cost of health care conversion will leave her with $14.00 in pension income. Her statement to us is perhaps the most poignant of this selected group. She says:

"$90.00 doesn't seem like much, but you get

> used to depending on it and it is important. But mostly my heart goes out to the people who need this far more than me. It's a damned shame that this had to happen, and my beloved husband would be outraged at this whole thing. Something must be done."

One retiree and his wife are confronting a family crisis. The wife was advised that she needs two operations. Their monthly pension is $503.23, and medical coverage costs $151.00 per month. Without the coverage Kaiser Steel provided, the family cannot pay for the needed operations.

Another retiree worked twenty-eight (28) years for Kaiser Steel and recently suffered a heart attack. Monthly insurance costs, which will not include Dental care or Major Medical benefits, of $151.00 represent 15 percent of his pension. Paying for health insurance, he says, will make it impossible to pay the property taxes owed on his home. Understandably, he and his wife are worried about the loss of their home and their future security.

We in the Union are proud of the accomplishments of our retired members and their spouses from Kaiser Steel and LTV Steel as well as other companies. We wholeheartedly agree with them that something must be done. Over 1,000 sworn statements from Kaiser retirees and their survivors detail the obstacles faced when people on limited, fixed incomes lose their employer-provided health benefits.

I join our President Lynn R. Williams in pledging our support for the Retiree Benefits Security Act of 1987. Kaiser Steel retirees and surviving spouses, as well as others, cannot be permitted to lose an entire lifetime of insurance protection.

Sincerely yours,

Robert R Guadiana

Robert R. Guadiana
Director, District 39

RRG:pg

cc: U. S. Senator Alan Cranston
U. S. Senator Pete Wilson

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LOUIS E. GELT
GREGORY C. TEVIS
OF COUNSEL

March 31, 1987

David Starr
Legislative Director of
The Honorable Howard Metzenbaum
United States Senate
Washington, D.C. 20510

Re: S 548

Dear Mr. Starr:

You have requested that we provide you with examples of the hardships which are being suffered by retirees of Kaiser Steel as a result of the Chapter 11 proceedings and the termination of medical benefits. What follows are examples which have been provided to me by that part of the subcommittee representing salaried retirees. I am informed that the hourly retirees will provide you with such examples directly through the United Steelworkers of America.

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**H. THOMAS AND LINDA HUDSON**

Mr. Hudson is 56 years old and has been retired for three years. He was in good health when he retired, but since has had five unsuccessful heart bypasses and is now on life-support machines at home, and cannot communicate well. Mrs. Hudson has an artificial leg. The Hudsons have lost their basic health care, their major medical care, their prescription drug plan, their vision care plan, and their $20,000 life insurance policy. The insurance carrier (New York Life Insurance Company -- "NYLIC") will not permit Mr. Hudson to continue to pay his own premiums. Mrs. Hudson writes "we for one are very effected by all of this, but then we are only one case of many who will suffer. My husband has been a very courageous person dealing with 'Lou Gehrig's Disease,' and knowing at least he was leaving me with a health plan and at least $20,000 insurance. This has only struck another blow to his once great belief in our so-called system of fairness to fellow man." Mrs. Hudson goes on to note that her husband took some pride in the feeling that he was at least leaving her with the medical support and financial capacity necessary to provide for herself while having an artificial limb, but that "now he feels that he has left nothing for his years of earning, and it hurts him deeply."

**JAMES STAMM**

Mr. Stamm is 78 years old and has been retired from Kaiser for 13 years. He has had Parkinson's Disease for the past 15 years and has been in a convalescent home for the past six years. His drug bill costs $400 per month. He has lost his major medical coverage, and now has to pay $150 per month for a basic medical plan. He has also lost his life insurance and must pay for all of his prescription drugs.

### TOM NICHOLSON

Mr. Nicholson is 65 years old, and his wife is 60. He worked for Kaiser for 30 years and has had a triple bypass and five strokes. He is dying of a heart disease known as "Subacute Bacterial Endocarditis," and also has poeumonia and kidney infection. His doctors say that he will live anywhere from a few days to a few months. He has lost his supplemental health care, his wife's basic health care, and each of their major medical care, prescription drug, vision care and life insurance policy.

### RICHARD W. WELSH

Mr. Welsh is 53, his wife is 50 and he worked for Kaiser for 23 years. He is not insurable because of a heart attack suffered in 1986 which was repaired by angioplasty. His wife is uninsurable because of breast cancer which occurred 10 years ago. Conversion rights from the Kaiser Group Plan to a New York Life Individual Plan have been offered, but are extremely expensive. The cost for the Welshes and their two dependent children for a substantially reduced amount of coverage would be $16,567.20 for 1987. This coverage would not include vision care or a prescription drug plan. Mr. and Mrs. Welsh have also lost their life insurance policy with NYLIC.

### SAM MORNING

Mr. Morning suffered a massive heart attack while working at Kaiser and retired on long-term disability in 1979 at 60 percent of his salary less his social security payment of approximately $1,200 per month. He is now 55 years old, and has applied to convert to a regular retirement package but was told that he will now receive only $749 per month as opposed to the $1,004 per month he would have received under prior conditions. In addition, he has lost all of his medical coverage, prescription drug coverage and life insurance. His monthly costs include $112 for prescriptions, $67 for medical insurance for his wife, $37 for a supplement to Medicare, and $88 per year for a $2,000 life insurance policy.

### NAME WITHHELD

This retiree, whose name has been withheld, is 61 years old, married, and worked for Kaiser for 25 years. He is now uninsurable because of a heart condition, and he and his wife have lost their basic health care, major medical care, prescription drug plan, vision plan, and a $33,000 life insurance policy. In addition, he is losing approximately $800 per month on his pension as a result of having continued to work for Kaiser, at Kaiser's request, for an additional two years after he was eligible for retirement, since Kaiser ultimately stopped purchasing annuities for its pensioners by the time he retired.

I hope this will provide you with a representative sampling of the hardships which are being suffered by Kaiser's salaried retirees as a result of the termination of benefit payments by Kaiser prior to the filing of the Chapter 11 petition. My clients would be very grateful if Congress would take action to protect them to the maximum extent possible under the circumstances. Please call if I can provide you with any further information.

Very truly yours,

Carl a Eklund
Carl A. Eklund

CAE:keg

Senator **Metzenbaum**. Are steelworkers at other companies concerned about possible termination of their health benefits? How prevalent is this concern? We hear a lot of talk about certain other companies that are on the brink of going into bankruptcy. Tell me, if you would, Mr. Williams, what are steelworkers throughout the country saying about the issues that are before us today?

Mr. **Williams**. Oh, the concern has just galvanized retired steelworkers into action right across America. We have been in the process in recent years of establishing an organization for our retirees called SOAR, and nothing has happened to bring people into SOAR that matches what is occurring in this concern about health care benefits.

It is not just, of course, steelworkers. It is pervasive right across industry in America. Certainly, you are quite correct, unfortunately, that a great number of steel companies have gone into bankruptcy. There are others that we are concerned about all the time, but there are many other industries, many other companies, many other retired workers are really very upset and very worried about what can happen to their health benefits.

It is also true of salaried workers. We were talking to some of the salaried workers out in the corridor before the hearing and joking that this issue has organized them in a way we were never able to organize them in the years that we were appealing to them to join the union. So there is enormous concern about this.

Senator **Metzenbaum**. On that point of the salaried workers, there is a rather interesting development. The salaried workers of LTV have hired a man as their attorney who headed up the Presidential campaign effort of no less a person than the well-renowned Senator Robert Taft—Robert Taft, Sr., of Taft-Hartley Act fame—to represent them. So I think we find in this that it is not political in any way. You find that it cuts right across political lines, and you find some of the most prominent members of both parties very strongly concerned, very much concerned about the issues that we have before us today.

Mr. **Williams**. That is entirely correct. As you have heard in your hearings and as you hear from your constituents constantly—and Senator Heflin, too—there simply is nothing more threatening to the peace of mind and the security of an older retired person than the thought that they are going to be without health care protection.

We know Medicare protection itself is less and less adequate with the enormous escalation there has been in health care costs, and even when they are eligible for Medicare—as many of these folks are not—still the threat to their security is just overwhelming.

Senator **Metzenbaum**. As you mentioned, I conducted a hearing about this in Cleveland, and I am frank to say that the stories that some of those retirees told me about their concerns, about their fears in losing their health benefits—and they had lost them at that time—actually brought tears to my eyes. It was a very, very emotional hearing. These are real people with real life problems.

Thank you very much, Mr. Chairman.

Senator **Heflin**. Mr. Williams, since we have a vote on shortly on the highway bill, the President's veto issue, I will not ask any other questions right now. I will submit, and any other members of the subcommittee can submit, questions. We would like to have those questions submitted by putting them in the mail through our subcommittee staff to you no later than April 8. In order to expedite this matter, we would like to request that the answers to the questions be put back in the mail by April 20.

There may be some other questions, but we would, therefore, have your answers to these questions by the time the second hearing is held.

Mr. Williams. Thank you. We will respond immediately when we receive the questions and certainly well within the time limits.

Senator Heflin. Thank you, sir.

Our next witness is Mr. Michael Holland of the United Mine Workers and Mr. Mike Nicholson who is associate general counsel, United Automobile Workers from Detroit.

I would suggest that if you have written statements, they be submitted for the record in full; and that each of you summarize and endeavor to complete your summary in 5 minutes.

### STATEMENTS OF A PANEL CONSISTING OF MICHAEL B. NICHOLSON, ASSOCIATE GENERAL COUNSEL, UNITED AUTO WORKERS, DETROIT, MI; AND MICHAEL H. HOLLAND, GENERAL COUNSEL, UNITED MINE WORKERS OF AMERICA, WASHINGTON, DC

Mr. Nicholson. I will try to do that, Mr. Chairman.

My name is Michael Nicholson. I am an associate general counsel for the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America. With me is Alan Reuther, another associate general counsel in our legislative office here in Washington, DC.

Senator Metzenbaum. Why do you not bring the mike a little closer.

Mr. Nicholson. OK. The UAW appreciates the opportunity to testify before the subcommittee concerning the proposed Retiree Benefits Security Act of 1987, and we urge the subcommittee to give prompt and favorable consideration to this piece of crucial legislation which we believe would help ensure that retirees are treated fairly in chapter 11.

The issue was brought to the forefront of public attention during the last Congress because of the situation at LTV Corporation which has already been discussed by the members and by President Williams. The interim legislation passed last year in response to the LTV crisis may have alleviated the immediate problem then facing the LTV retirees, but it did not resolve the basic issues raised by LTV's original actions, since the health and life insurance of LTV retirees, including the thousands of UAW members retired from LTV's aerospace units, are still at risk.

Moreover, this problem does not only affect the retirees of the LTV Corporation. Other companies in chapter 11 have threatened to cut off the health insurance benefits of their retirees, and still other companies, such as the Allis Chalmers Corporation where there are thousands of UAW retirees, have threatened to file for relief under the bankruptcy code as a way of coercing retirees into substantial reductions in their hard-earned insurance benefits.

It is, therefore, of the utmost importance that the bankruptcy code be amended to clearly protect the benefits of these retired American workers, whether union or nonunion, so that situations like these do not continue to occur.

The legislation which has been introduced by Senator Metzenbaum and the other Senators would provide a fair and comprehensive solution to the problem of how retiree benefits should be treated under the bankruptcy code.

First, the bill would amend section 1113(f) to clarify that this provision applies to all benefits provided under a collective bargaining agreement, including the benefits of retired employees as well as those of active workers. This amendment would simply make clear Congress' original intent when section 1113 was enacted that the protections afforded by section 1113(f) against unilateral modification or termination of collectively bargained benefits apply to all such benefits, regardless of whether they might be considered pre- or post-petition claims.

This clarification of section 1113(f) would mean that the collectively bargained benefits of retirees, like those of active workers, remain an enforceable employer obligation after the filing of a bankruptcy petition. An employer must first bargain with the union concerning contract modifications before the employer can seek court permission to reject its collective bargaining agreement. And such agreements may be rejected only if the court finds that the bargaining has resulted in an impasse, and that the modifications and benefits proposed by the employer are necessary to enable the company to continue in business and are fair and equitable to all the parties. As clarified, section 1113(f) would unmistakably provide that an employer cannot terminate or alter any collectively bargained promises without complying with these section 1113 procedures.

Second, the legislation would add a new section 1114 to the Bankruptcy Code, which would extend protection against unilateral termination or modification of retirement insurance benefits to all retirees, without regard to whether they are covered by a collective bargaining agreement. Section 1114 would also require the court to appoint representatives for nonunion retirees who would protect their interests and be able to join in out-of-court negotiations with the debtor over possible modifications in the retirement insurance benefits of such nonunion retirees.

Third, the new section 1114 would also provide, with respect to all retirees, that an employer can modify retiree insurance benefits, absent a negotiated settlement, only if the court authorizes such modifications after finding that they are necessary to enable the company to continue in business and are fair and equitable to all the parties. Employers would be precluded from taking the position that a court order permitting rejection of a collective bargaining agreement eliminates the obligation to provide union retirees with any retirement insurance benefits. Instead, as with nonunion retirees, employers would have to continue paying insurance benefits to union retirees at whatever reduced level was determined by the court to be necessary to allow the company to continue in business and be fair and equitable. In addition, both before and after any court-ordered modifications, employers would be required to pay the appropriate retiree insurance benefits as an expense of administration, the same priority given to the wages and benefits of employees working for the debtor.

Fourth, the legislation would provide that retirees will be treated as a separate class for purposes of voting on any plan of reorganization. This provision is designed to ensure that the debtors negotiating a plan of reorganization with various other creditors must also negotiate with the retirees so that retirees will have a voice in any plan of reorganization. This will effectively prevent plans of reorganization from being used as mere devices to discharge and eliminate the retiree insurance coverage which is so crucial to the elderly.

Finally, the legislation provides that a plan of reorganization cannot be deemed accepted by the creditors over the objection of the class of retirees unless the court determines that the plan will only result in "the minimum reduction in retiree benefits consistent with the ability of the debtor to provide such benefits after confirmation of the plan." This provision ensures that the other creditors are not allowed to run roughshod over the interests of the retirees, and that retiree insurance benefits will be continued under any plan of reorganization at whatever level can be afforded by the company.

While the proposed Retiree Benefits Security Act recognizes the unique interests of retirees in bankruptcy proceedings, it does not grant retirees a veto power over any plan of reorganization or guarantee that their benefits cannot be modified regardless of the economic circumstances of the employer. Instead, the proposed legislation recognizes that the Bankruptcy Code is designed to ensure that the interests of all creditors are treated fairly, and that troubled companies are given a fair opportunity to reorganize.

The UAW is acutely aware that the interests of retirees must be balanced against these other interests. We submit, however, that the Retiree Benefits Security Act would strike the proper balance, and ensure that both union and nonunion retirees, as well as the debtor, its creditors and its employees, are treated fairly and equitably in any bankruptcy proceedings.

In conclusion, the UAW urges this subcommittee to give prompt, favorable consideration to the proposed legislation, and we will look forward to working with the members of this subcommittee as you deal with these important issues.

Thank you very much.

[The following material was submitted for the record:]

# SUMMARY STATEMENT OF MICHAEL B. NICHOLSON ASSOCIATE GENERAL COUNSEL, INTERNATIONAL UNION, UAW ON THE RETIREE BENEFITS SECURITY ACT OF 1987 (S. 548) BEFORE THE SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE OF THE COMMITTEE ON THE JUDICIARY, U. S. SENATE

When LTV Corporation filed for Chapter 11 on July 17, 1986, it cut off all payments for retiree health and life insurance benefits. This action raised a serious threat to the well-being of tens of thousands of LTV retirees and their families, including several thousand retired UAW members from LTV Aerospace and Defense Corportion. Other companies, such as A. H. Robins Company and Allis Chalmers, have also threatened to take similar actions. Thousands of retirees are looking to Congress to enact permanent legislation which will ensure that the bankruptcy laws are not used as a device to deprive them of the health and life insurance coverage they so desperately need in their retirement years.

The UAW strongly supports the proposed Retiree Benefits Security Act of 1987 (S. 548), and urges the Subcommittee to give this bill prompt, favorable consideration. We believe this legislation would help ensure that retirees are treated fairly in Chapter 11 reorganization proceedings.

First, the bill would amend Section 1113(f) of the Bankruptcy Code to clarify that this provision applies to all benefits provided under a collective bargaining agreement, including the benefits of retired employees as well as those of active workers.

Second, the legislation would add a new Section 1114 to the Bankruptcy Code, which would extend protection against unilateral termination or modification of retirement insurance benefits to all retirees, without regard to whether they are covered by a collective bargaining agreement.

Third, the new Section 1114 would also provide, with respect to all retirees, that an employer can modify retiree insurance benefits, absent a negotiated settlement, only if the court authorizes such modifications after finding that they are necessary to enable the company to continue in business and are fair and equitable to all parties. Both before and after any court-ordered modifications, employers would be required to pay the appropriate retiree insurance benefits as an expense of administration, the same priority given to the wages and benefits of the employees working for the debtor.

Fourth, the legislation also provides that retirees shall be treated as a separate class for purposes of voting on any plan of reorganization. This provision is designed to ensure that debtors negotiating a plan of reorganization with various other creditors must also negotiate with their retirees, so that the retirees will have a voice in any plan of reorganization.

The UAW submits that the special treatment afforded to the claims of retirees under the proposed Retiree Benefits Security Act is entirely appropriate. The courts have generally recognized that retiree benefits are vested, lifetime benefits which may not be reduced once an employee (whether union or nonunion) retirees. In addition, retired workers also occupy a very different position from other creditors of an employer in bankruptcy proceedings, and therefore should be accorded special treatment which takes account of this fact.

Mr. Chairman. I am Michael B. Nicholson, an Associate General Counsel for the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America (UAW). The UAW appeciates the opportunity to testify before this Subcommittee concerning the proposed Retiree Benefits Security Act of 1987 (S. 548). We urge this Subcommittee to give prompt, favorable consideration to this crucial legislation, which would help ensure that retirees are treated fairly in Chapter 11 reorganization proceedings.

At the end of the last Congress, the House and Senate passed interim legislation which requires employers filing for relief under the Bankruptcy Code to continue paying all health and life insurance, sickness, accident and disability benefits due retired former employees until May 15, 1987. This interim legislation was enacted with bipartisan support, in order to give Congress time to consider and act on the broader issue of how retiree benefits should be treated under the Bankruptcy Code.

This issue was brought to the forefront of public attention during the last Congress because of the situation at LTV Corporation, which filed petitions under Chapter 11 of the Bankruptcy Code for itself and its subsidiaries on July 17, 1986. On that same date, LTV cut off all payments for the medical bills of its hourly and salaried retirees from its self-insured health plans, and also stopped payment of premiums for retiree life insurance. LTV claimed that this was "because of the restraints imposed by Chapter 11."

This action raised a serious threat to the well-being of tens of thousands of LTV retirees and their families, including several thousand retired UAW members from LTV Aerospace and Defense Corporation. Because LTV refused to pay any medical bills for retirees after July 17, 1986, even for services that had already been performed, many retirees were stuck with huge medical bills. Furthermore, all of the retirees suddenly faced the prospect of having to pick up the cost of their health and life insurance coverage, an enormous burden for most retirees.

Legislation was quickly introduced in Congress in response to the crisis created by LTV's actions. As a result of this legislative initiative, and as a result of effective strike action by the Steelworkers Union, LTV was forced to modify its position. On July 30, 1986, it went to the Bankruptcy Court and obtained permission to reinstate the health and life insurance coverage for retirees retroactively, and to continue that coverage for six months.

But while this step may have alleviated the immediate problem then facing the LTV retirees, it did not resolve the basic issues raised by LTV's original actions, since the health and life insurance benefits of LTV retirees are still at risk. Moreover, this problem does not only affect retirees of the LTV Corporation. Other companies in Chapter 11, such as the A.H. Robins Company, have threatened to cut off the health insurance benefits of their retirees. And still other companies, such as Allis-Chalmers Corporation, have threatened to file for relief under the Bankruptcy Code as a way of coercing retirees into substantial reductions in their hard earned insurance benefits. It is, therefore, of the utmost importance that the Bankruptcy Code be amended to clearly protect the benefits of retired American workers, whether union or nonunion, so that situations like the LTV crisis do not continue to occur.

The legislation which has been introduced by Senator Metzenbaum, along with many other Senators on both sides of the aisle, would provide a fair and comprehensive solution to the problem of how retiree benefits should be treated under the Bankruptcy Code.

First, the bill would amend Section 1113(f) to clarify that this provision applies to all benefits provided under a collective bargaining agreement, including the benefits of retired employees as well as those of active workers. This amendment would simply make clear Congress' original intent when Section 1113 was enacted that the protections afforded by Section 1113(f) against unilateral modification or termination of collectively bargained benefits apply to all such benefits, regardless of whether they might be considered pre or post petition claims.

This clarification to Section 1113(f) would mean that the collectively-bargained benefits of retirees, like those of active workers, remain an enforceable employer obligation after the filing of a bankruptcy petition. An employer must first bargain with the union concerning contract modifications before the employer can seek court permission to reject its collective bargaining agreement. And such agreements may be rejected only if the court finds that the bargaining has resulted in an impasse, and that the modifications in benefits proposed by the employer are necessary to enable the company to continue in business and are fair and equitable to all parties. As clarified, Section 1113(f) would unmistakably provide that an employer cannot terminate or alter any collectively bargained contract promises without complying with these Section 1113 procedures.

Second, the legislation would add a new Section 1114 to the Bankruptcy Code, which would extend protection against unilateral termination or modification of retirement insurance benefits to all retirees, without regard to whether they are covered by a collective bargaining agreement. Section 1114 would also require the court to appoint representatives for nonunion retirees, who would protect their interests and be able to join in out-of-court negotiations with the debtor over possible modifications in the retirement insurance benefits of such nonunion retirees.

Third, the new Section 1114 would also provide, with respect to all retirees, that an employer can modify retiree insurance benefits, absent a negotiated settlement, only if the court authorizes such modifications after finding that they are necessary to enable the company to continue in business and are fair and equitable to all parties. Employers would be precluded from taking the position that a court order permitting rejection of a collective bargaining agreement eliminates the obligation to provide union retirees with any retirement insurance benefits. Instead, as with nonunion retirees, employers would have to continue paying insurance benefits to union retirees at whatever reduced level was determined by the court to be necessary to allow the company to continue in business and to be fair and equitable to all parties. In addition, both before and after any court-ordered modifications, employers would be required to pay the appropriate retiree insurance benefits as an expense of administration, the same priority given to the wages and benefits of the employees working for the debtor.

Fourth, the legislation provides that retirees shall be treated as a separate class for purposes of voting on any plan of reorganization. This provision is designed to ensure that debtors negotiating a plan of reorganization with various other creditors must also negotiate with their retirees so that the retirees will have a voice in any plan of reorganization. This will effectively prevent plans of reorganization from being used as mere devices to discharge and eliminate the retiree insurance coverage which is so crucial to the elderly.

The legislation also specifies that the claims of active workers and retirees covered under Sections 1113 and 1114 which would be payable under a plan of reorganization shall not be limited by the one-year limit on damages in Section 502(b)(7) of the Bankruptcy Code. This provision codifies the court decisions which hold that Section 502(b)(7) was simply intended to prevent highly paid executives from collecting on golden parachute-type contracts with the debtor, not to limit the claims of rank-and-file workers and retirees. See, **In re Gee & Missler Services, Inc.**, 62 B.R. 841 (Bankr. E.D. Mich. 1986). But see **In re Cortland Container Corp.**, 30 B.R. 715 (Bankr. N.D. Ohio 1983). This provision is particularly important for retirees, since they typically have been contractually promised insurance benefits for life, in return for which they have rendered a lifetime of service to their former employer.

The legislation also provides that any benefits paid to retirees during the pendency of the Chapter 11 proceedings may not be used to offset whatever amounts are coming to the retirees under a plan of reorganization. Again, this provision is needed to ensure that the amounts paid on retiree claims under a plan of reorganization are not diluted during the bankruptcy proceedings.

Finally, the legislation provides that a plan of reorganization cannot be deemed accepted by the creditors over the objection of the class of retirees, unless the court determines that the plan will only result in "the minimum reduction in retiree benefits consistent with the ability of the debtor to provide such benefits after confirmation of the plan." This provision ensures that the other creditors are not allowed to run roughshod over the interests of the retirees, and that the retiree insurance benefits will be continued under any plan of reorganization at whatever level can be afforded by the company.

The UAW submits that the special treatment afforded to the claims of retirees under the "Retiree Benefits Security Act" is entirely appropriate. The courts have generally recognized that retiree benefits are vested, lifetime benefits which may not be reduced once an employee (whether union or nonunion) retires. Since the retiree has rendered all of his or her promised services to the employer, upon retirement he or she is entitled to get the benefits the employer has promised, and the employer may not renege on its commitment.

Retired workers (whether union or nonunion) also occupy a very different position from other creditors of an employer in bankruptcy proceedings, and therefore should be accorded special treatment which takes account of this fact. Most creditors in bankruptcy proceedings, such as banks and suppliers, can afford to wait for the reorganization or liquidation to be completed before receiving payment on their claims. The banks have made many loans, the suppliers have many customers. In the normal course of business, they can expect that a few borrowers and customers will encounter economic difficulties and have to delay or not make their payments at all. This is a normal, expected cost of doing business, which can usually be absorbed and passed on to other borrowers and customers.

The situation of retirees is fundamentally different. Retirees cannot obtain health or life insurance from another employer. And they do not have the bargaining leverage of other "players" in the bankruptcy process - such as bankers and suppliers who have ongoing relationships with the debtor - which can ensure fair treatment during the bankruptcy case, and after its conclusion. Moreover, with their limited budgets, retirees cannot easily absorb the heavy insurance costs they may find themselves saddled with upon the filing of a Chapter 11. And they cannot pass these costs along to any other parties.

In addition, retirees cannot afford to wait months or years while the courts sort things out. Retirees often have urgent medical needs which require immediate attention. As a result, they may incur large hospital and medical bills which must be paid immediately. And even in those situations where medical care can be postponed, the anxiety generated by the possibility of having uninsured catastrophic health care costs hanging over their heads inevitably takes a heavy toll on retirees.

While the proposed Retiree Benefits Security Act recognizes the unique interests of retirees in bankruptcy proceedings, it does not grant retirees a veto power over any plan of reorganization or guarantee that their benefits cannot be modified regardless of the economic circumstances of the employer. Instead, the proposed legislation recognizes that the Bankruptcy Code is designed to ensure that the interests of all creditors are treated fairly, and that troubled companies are given a fair opportunity to reorganize. The UAW is acutely aware that the interests of retirees must be balanced against these other interests. We submit, however, that the Retiree Benefits Security Act would strike the proper balance, and ensure that both union and nonunion retirees, as well as the debtor, its creditors and its employees, are treated fairly and equitably in any bankruptcy proceedings.

In conclusion, the UAW urges this Subcommittee to give prompt, favorable consideration to the proposed Retiree Benefits Security Act (S. 548). Thousands of retirees are looking to the Congress to ensure that they are treated fairly under the bankruptcy laws, and that such laws are not used as a basis for depriving them of the health and life insurance coverage they so desparately need in their retirement years. The legislation which is before this Subcommittee would accomplish that result.

Mr Chairman, the UAW appreciates the opportunity to present our views on this crucial legislation. We look forward to working with the Members of this Subcommittee as you deal with these important issues.

Thank you.

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**INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE & AGRICULTURAL IMPLEMENT WORKERS OF AMERICA—UAW**

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*Associate General Counsel*
*Special Counsel*
JOHN A. FILLION

April 22, 1987

Senator Howell Heflin, Chairman
Subcommittee on Courts &
Administrative Practice
United States Senate Committee
on the Judiciary
Washington, D.C. 20510

Dear Senator Heflin:

Thank you for giving the UAW an opportunity to testify in support of the Retiree Benefits Security Act at the April 1, 1987 hearings before your Subcommittee.

After the hearing, we received various questions submitted by members of the Subcommittee. I have enclosed with this letter a listing of the questions submitted along with our answers. We hope this additional information is helpful.

Again, thank you for your invitation to participate in the hearings and for your support of this critical legislation.

Very truly yours,

Michael B. Nicholson

MBN:jv
opeiu494
cc: Alan Reuther

## QUESTIONS FOR MIKE NICHOLSON, UNITED AUTO WORKERS

1. SECTIONS 1113(h) AND (i) OF S.548 PROVIDE THAT A UNION CAN DECLINE TO SERVE AS THE AUTHORIZED REPRESENTATIVE OF THE RETIREES. UNDER WHAT CIRCUMSTANCES MIGHT YOU EXPECT THE UNION TO DECLINE?

   The Second Circuit's recent decision in **UAW v. Century Brass Products, Inc.**, 795 F.2d 265 (2d Cir. 1986), cert. denied, ___ U.S. ___, 107 S.Ct. 433, discusses circumstances in which separate representation for retirees for negotiation purposes would be appropriate.

2. COULD A SITUATION ARISE WHERE THE UNION WANTS TO REPRESENT RETIREES, BUT SOME RETIREES DON'T BELIEVE THE UNION WILL DO A GOOD JOB REPRESENTING THEIR INTERESTS? IN SUCH A CASE, COULD SOME RETIREES "OPT OUT" OF REPRESENTATION BY THE UNION?

   Section 1113(h) and (i) of S.548 do not provide for retirees to "opt out" of representation by the union in situations where the union has not declined to serve as the authorized representative of the retirees.

3. THE UNION'S PRIMARY RESPONSIBILITY IS TO CURRENT EMPLOYEES. WHEN "PUSH COMES TO SHOVE", HOW CAN THERE **NOT** BE A CONFLICT OF INTEREST WHERE THE REPRESENTATIVE OF THE RETIREES ALSO REPRESENTS CURRENT EMPLOYEES? (FOR EXAMPLE, CURRENT EMPLOYEES MAY BE OUT OF A JOB DUE TO A CHAPTER 7 LIQUIDATION -- WHICH IS PRECIPITATED BY THE PAYMENT OF THESE BENEFITS).

   As noted, the Second Circuit's decision in **UAW v. Century Brass Products, Inc.**, 795 F.2d 265 (2d Cir. 1986), cert. denied, ___ U.S. ___, 107 S.Ct. 433, discusses the possibility of such conflicts of interest. Significantly, the Second Circuit found that nonetheless retirees "are generally capable of being represented by the union as their 'authorized representative.'" 795 F.2d at 275. In other words, the Second Circuit found that in most cases, such a conflict of interest with employees does not exist.

* * *

**Senator Thurmond**

QUESTIONS FOR UNION PANEL: **(Messrs. Holland, Nicholson)**

1. I FEEL THAT ANY LEGISLATION WHICH THE CONGRESS PASSES MUST INSURE THAT UNION AND NON-UNION RETIREES ARE TREATED EXACTLY THE SAME IN CHAPTER 11 PROCEEDINGS. DO YOU BELIEVE THAT S.548, AS CURRENTLY DRAFTED, INSURES THAT RESULT?

   Yes.

2. THIS LEGISLATION ALLOWS THE LABOR ORGANIZATION WHICH REPRESENTS EMPLOYEES COVERED BY A COLLECTIVE BARGAINING AGREEMENT TO CHOOSE TO BECOME THE AUTHORIZED REPRESENTATIVE OF THOSE RETIREES RECIEVING BENEFITS COVERED BY THAT AGREEMENT. GIVEN THAT THE INTERESTS OF CURRENT EMPLOYEES AND RETIREES ARE HARDLY IDENTICAL,

DOES NOT THIS PROVISION OF THE LEGISLATION CREATE A POTENTIAL CONFLICT OF INTEREST FOR THE LABOR ORGANIZATION IF IT ELECTS TO BECOME THE AUTHORIZED REPRESENTATIVE?

As noted, the Second Circuit's decision in **UAW v. Century Brass Products, Inc.,** 795 F.2d 265 (2d Cir. 1986), cert. denied, ___ U.S. ___, 107 S.Ct. 433, discusses the possibility of such conflicts of interest. Significantly, the Second Circuit found that nonetheless retirees "are generally capable of being represented by the union as their 'authorized representative.'" 795 F.2d at 275. In other words, the Second Circuit found that in most cases, such a conflict of interest with employees does not exist.

* * *

## QUESTIONS FOR THE UNION PANEL

1. S.548 WOULD AMEND SECTION 1113(f) BY ADDING THE LANGUAGE "INCLUDING ANY PROVISION RELATING TO BENEFITS FOR RETIRED EMPLOYEES." WOULD THIS LANGUAGE INCLUDE PENSION BENEFITS? IS THIS NOT IN CONFLICT WITH LEGISLATION PASSED AS A PART OF THE RECONCILIATION BILL LAST YEAR WHICH PROVIDED THAT TO TERMINATE PENSION BENEFITS, A COMPANY HAD TO COMPLY WITH THE ERISA LAWS? DOES THIS NOT SEVERELY IMPACT UPON A COMPANY'S ABILITY TO REORGANIZE?

   The language to be added by S.548 to Section 1113(f) would make it clear that Section 1113(f) includes within its protection all collectively bargained benefits, including pension benefits. This is not in conflict with the Single Employer Pension Plan Amendments Act (SEPPAA). SEPPAA establishes certain requirements and procedures which must be satisfied before a single-employer defined benefit pension plan may be terminated. But SEPPA does not change or free an employer from its collectively bargainined obligations with respect to such plans. Conversely, Section 1113 governs the manner in which employers may seek relief from such bargained obligations including those related to pension benefits. The proposed amendment to Section 1113(f) would clarify current law, and would not severely impact upon a company's ability to reoganize.

2. THE LANGUAGE OF PROPOSED SECTION 1113(g) EXEMPTS ALL CLAIMS ARISING UNDER ANY COLLECTIVE BARGAINING AGREMENT COVERED BY SECTION 1113 FROM THE ONE-YEAR LIMIT IN DAMAGES IN SECTION 502(b)(7). DOES THIS EXEMPTION FROM 502(b)(7) EXTEND ONLY TO CLAIMS INVOLVING MEDICAL AND INSURED BENEFITS, OR IS THE LANGUAGE ALL INCLUSIVE? IS THE STANDARD THE SAME FOR UNION AND NON-UNION EMPLOYEES? RETIRED AND CURRENT EMPLOYEES?

   The language in proposed Section 1113(g) extends to all claims arising under any agreement covered by Section 1113, and codifies the court decisions which hold that Section 502(b)(7) of the Bankruptcy Code was simply intended to prevent high paid executives from collecting on golden parachute-type contracts with the debtor, not to limit the claims of rank and file workers or retirees. See, **In re Gee & Missler Services, Inc.,** 62 B.R. 841 (Bankr. E.D. Mich. 1986). But see **In re Cortland**

Container Corp., 30 B.R. 715 (Bankr. N.D. Ohio 1983). In other words, such decisions hold that Section 502(b)(7) was not intended to limit the claims of any persons arising under a collective bargaining agreement, whether active or retired. The proposed Section 1114(i) provides a similar codification with respect to the benefits covered by Section 1114. Thus, Section 1113, as amended by S.548, and proposed Section 1114 would make clear that Section 502(b)(7) does not limit the claims of any persons arising under contracts covered by Section 1113 or benefits covered by Section 1114, without regard to the union or non-union status of such persons.

3. WHAT POLICY CONSIDERATIONS DICTATE ESTABLISHING RETIREES AS A SEPARATE CLASS FOR PURPOSES OF VOTING ON A PLAN OF REORGANIZATION, AND HOW WILL THIS AFFECT THE RIGHTS OF OTHER UNSECURED CREDITORS?

   Establishing retirees as a separate class for purposes of voting on a plan of reorganization is dictated by the need to give retirees a greater voice in the negotiation and implementation of the plan of reorganization, the most important step in any Chapter 11 proceeding. This step does not adversely affect the rights of other creditors, because S.548 specifically does not give retirees a veto power over any plan of reorganization, by virtue of the provisions set forth in the proposed amendments to Section 1129 of the Bankruptcy Code.

4. IF THE RECOGNIZED EXCLUSIVE COLLECTIVE BARGAINING REPRESENTATIVE OF THE EMPLOYEES ELECTS NOT TO SERVE AS THE AUTHORIZED REPRESENTATIVE, THE COURT SHALL APPOINT A COMMITTEE OF RETIRED EMPLOYEES.

   (A) IF A COMPANY HAS RETIRED WORKERS WHO ARE COVERED BY A COLLECTIVE BARGAINING AGREEMENT, AND WORKERS WHO ARE NOT COVERED BY A COLLECTIVE BARGAINING AGREEMENT, WOULD THIS LEGISLATION ESTABLISH TWO SEPARATE COMMITTEES OF RETIRED EMPLOYEES?

   (B) HOW LARGE WILL THIS COMMITTEE BE IN TERMS OF PROVIDING REPRESENTATION FOR THE RETIRED WORKERS?

   (C) WILL THE COMMITTEE BE AUTHORIZED TO HIRE ATTORNEYS AS OTHER UNSECURED CREDITOR COMMITTEES ARE ALLOWED TO DO? WHAT ARE THE POWERS OF THE RETIREES' COMMITTEE?

   (A) S.548 leaves to the discrection of the court the question of whether to appoint separate committees for the varying groups of retired employees, or to appoint one committee.

   (B) S.548 also leaves to the discretion of the court the size of the committee to be appointed as the representative for the retired workers.

   (C) While S.548 is silent as to the question of whether the retirees committee should be authorized to hire attorneys compensated by the estate, as with unsecured creditors committees it would be appropriate for the legislation to provide that retirees' committees should have such power. Retirees' committees should also have the power to enforce the provisions of Sections 1113 and 1114 with respect to the retired employees, and to take legal action to ensure that the debtor's obligations to the retired employees are met.

5. IT IS MY UNDERSTANDING THAT THE POWER TO REJECT A COLLECTIVE BARGAINING AGREEMENT UNDER SECTION 1113 OF

TITLE 11 OF THE CODE DOES NOT CARRY WITH IT A CORRESPONDING POWER OF MODIFYING THE AGREEMENT AS REJECTED, LEAVING THE PARTIES FREE TO RENEGOTIATE. THIS BILL SEEMS TO CHANGE THAT POLICY BY ALLOWING FOR MODIFICATION SECTION 1114(e) AND (f), BUT REQUIRING THE COURT, AT THE SAME TIME, NOT TO SET THE LEVEL BELOW THAT RECOMMENDED TO ALLOW THE COMPANY TO CONTINUE IN BUSINESS AND THAT WHICH IS FAIR AND EQUITABLE TO ALL PARTIES.

Section 1113 as presently codified does not give the debtor the power to unilaterally modify its collective bargaining agreement with a union. Instead, such an agreement can be modified only by mutual agreement. Where such agreement is not forthcoming, and if the debtor shows that it has met the standards for rejection of a collective bargaining agreement under Section 1113, then the court may enter an order providing that the agreement is rejected. Under current law, following rejection the parties are free to renegotiate a collective bargaining agreement.

S.548 would change this policy solely with respect to insurance benefits of retirees by requiring the debtor to continue to pay these benefits, even after rejection of the collective bargaining agreement, at a level which the court has determined is necessary to allow the company to continue in business and which is fair and equitable to all parties. In doing so, the bill recognizes that the benefits of persons already retired are generally vested, and need not be renegotiated in each collective bargaining agreement in order to continue. See **Allied Chemical and Alkali Workers v. Pittsburgh Plate Glass**, 404 U.S. 157 (1971). Moreover, S.548 recognizes that the National Labor Relations Board has continually held that, unlike benefits for active workers, benefits for persons already retired are **not** a mandatory bargaining subject over which employees have the right to strike without being discharged by their employer. Thus, the bill requires the debtor to continue paying retiree insurance benefits at the level found by the court to be necessary, fair and equitable, instead of leaving these retiree benefits hostage to future negotiations, and the possibility that employees will be threatened with discharge should they strike in order to compel the debtor to continue such benefits at even a modified level. In short, S.548 recognizes the special position of retiree benefits in collective bargaining, and provides appropriate protection to retirees while allowing debtors to modify those benefits to a level necessary to permit reorganization of the debtor.

6. S. 548 REQUIRES EMPLOYERS TO PAY RETIREES INSURANCE BENEFITS AS AN EXPENSE OF ADMINISTRATION. I HAVE TWO QUESTIONS:

(A) WILL THIS CREATE SUCH A BURDEN ON THE DEBTOR COMPANY THAT IT WILL PREVENT REORGANIZATION UNDER CHAPTER 11?

(B) WHY IS IT NECESSARY TO PROVIDE THESE EXPENSES AS ADMINISTRATION EXPENSES?

(A) Requiring debtors to pay retiree insurance benefits as an expense of administration does not create such a burden on the debtor company that it will prevent reorganization under Chapter 11, since S.548 also provides a mechanism for such benefits to be modified to a level which will permit a Chapter 11 reorganization.

(B) It is necessary to provide that retiree insurance benefits payable during the administration of the Chapter 11 case are administrative expenses because employers, such as LTV, have argued that Chapter 11 as presently constituted prohibits the payment of benefits to persons already retired precisely because they are not an expense of administration under the Bankruptcy Code.

7. IF THESE BENEFIT PAYMENTS ARE TREATED AS ADMINISTRATIVE EXPENSES, WHY IS IT NECESSARY TO ESTABLISH THE RETIRED WORKERS AS A SEPARATE CLASS FOR PURPOSES OF CONFIRMING A PLAN OF REORGANIZATION UNDER SECTION 1129?

It is necessary to establish the retired workers as a separate class for purposes of plan confirmation under Section 1129, notwithstanding the treatment of benefit payments as an administrative expense, because plan confirmation deals with a separate time period - i.e., the time after which a plan is confirmed and after which there are typically no administrative expenses, because the estate is no longer being administered under Chapter 11. The amendments to Section 1129 proposed in S.548 deal with the post-confirmation time period, and require that such benefits continue to be provided at a level that can be afforded by the reorganized debtor.

8. WHAT IS THE EFFECT AND PURPOSE OF SECTION 1114(h) OF THIS LEGISLATION WHICH WOULD PREVENT THE DEBTOR FROM OFFSETTING PAYMENTS OF HEALTH AND MEDICAL BENEFITS MADE DURING THE TIME OF FILING OF THE PETITION AND CONFIRMATION FROM PAYMENTS THAT WILL BE PAID AS PART OF THE PLAN OF REORGANIZATION?

Section 1114(h) of S.548 does not provide for double counting of claims for retiree benefits. Instead, it merely provides that amounts paid during administration of the estate will not be deducted from amounts which remain to be paid, such as claims for future benefits and claims for benefits which have not been paid as a result of court ordered modification of retiree benefits.

Senator HEFLIN. All right, sir. Mr. Holland, if you will, try to keep it to 5 minutes. I am going to have to wield the gavel.

## STATEMENT OF MICHAEL H. HOLLAND

Mr. HOLLAND. Thank you very much, Mr. Chairman.

My name is Michael Holland. I am the general counsel of the United Mine Workers of America, and on behalf of our International Union President Richard Trumka, I appreciate the opportunity to be here today to echo the comments made by the steelworkers and the auto workers in support of Senate bill 548.

The majority of the members, active coal mining members of the mine workers are second, third, and fourth generation coal miners. They have been employed in the coal industry for decades and live in the same coal field communities of their parents and grandparents. There are, therefore, very close personal ties between our active workers and members and our retiree members.

In addition, unlike many other unions, the retirees in the mine worker system are full members of the union. They are permitted to vote for officers at the international, the district and local union levels. They can serve as many officers in this union. They actively participate in our political action and legislative committee programs. And most importantly, retirees as union members participate as duly elected delegates to union conventions.

In that capacity they help formulate the union's position on collective bargaining issues. Moreover, they act as, in some cases, elected representatives of their local unions in our internal collective bargaining conferences which further fine-tune the union's bargaining demands.

In short, retirees under the mine worker system have both a close personal and constitutional tie with the active members of our union. Like the steelworkers and the auto workers, the LTV bankruptcy and its accompanying unilateral rejection of the retirees' health benefits sent shock waves through the coal field areas of the United States.

In my years of representing the union, both from a local union district and international level, I have never seen such an enormous and devastating response as was occasioned by the LTV bankruptcy.

The mine workers endorse and support and urge speedy adoption of Senate bill 548. We particularly applaud the provisions of that bill which classify postpetition payments of retiree benefits as administrative expenses. These provisions also preclude setoff for benefits paid postpetition, but prior to a reorganization plan's confirmation, from unpaid future benefits unless such a setoff is agreed by the debtor and the authorized representative of the retirees.

UMWA retirees' health benefits are part of our collective bargaining agreement. Our members feel strongly that they be accorded the same legal status that the Bankruptcy Act confers upon other collectively bargained benefits. Opponents of this legislation will counsel our pensioners to take their place in line with other creditors, both secured and unsecured, of the bankrupt company. They will tell you that the retirees' claims should be accorded no more priority than any other prepetition claim, professing that they arise out of a prepetition agreement and were earned wholly during the prepetition period. Such a view misperceives, we feel, the fundamental nature of the labor which is performed by employees during a postpetition period. It ignores the indisputable fact that retiree health benefits are part and parcel of the *quid pro quo* for the labor a debtor's employees provide after a petition has been filed.

Retirees should assume the same status as other parties willing to provide those services necessary to keep the company afloat, protect its assets, and prevent liquidation—all to the benefit of the company's creditors. The debtor in possession is a separate legal entity that is carrying on its business principally on behalf of the prefiling creditors.

When a debtor's employees are induced to continue supplying their services, the law should clearly require that their remuneration be accorded the status of administrative costs. For any claims incident to the debtor in possession's continued operation of the business, those must too be paid before the claims of the creditors for whose benefit the continued operation of the business is being conducted.

A final comment. In the real world context of collective bargaining in our union, wages and health benefits for active workers and health benefits for retired workers are indistinguishable at the bargaining table. Active members, laid-off members and retired members sit side by side if you will, and give our union negotiating teams "marching orders" with respect to their bargaining priorities.

In preparing for collective bargaining, all of our members—active, laid-off and retired—sit side by side and usually engage in the exercise of dividing up the "economic pie" as a manner of giving our officers direction on collective bargaining. That economic pie has slices for wages, vacation pay, disability pay, current and future pensions, and health benefit levels for actives and retirees.

Allocations are made for each category. The larger the slice of the pie for wages, the corresponding smaller size the other slices for other levels of benefits are.

My union's mindset, as we enter into collective bargaining, is that during the course of the subsequent contract term the labor of the active workers is exchanged for current wages, existing pension levels, future pensions and current health benefits for both actives and retirees.

In short, the consideration, the glue of the deal of the collective bargaining agreement continues to flow during the course of that contract, including those periods that are postpetition, and a very real part of the union's benefit of the bargain are the health benefits for the retirees who, in most cases, as I noted earlier, are family members of active workers in the United Mine Workers of America.

I appreciate the opportunity the committee has afforded the union to present that testimony and urge the committee and the Senate's adoption of S. 548. Thank you.

[Statement follows:]

## STATEMENT OF
## MICHAEL H. HOLLAND
## GENERAL COUNSEL
## UNITED MINE WORKERS OF AMERICA

MR. CHAIRMAN:

MY NAME IS MICHAEL H. HOLLAND. I AM THE GENERAL COUNSEL OF THE UNITED MINE WORKERS OF AMERICA. I AM HERE ON BEHALF OF THE UNION'S INTERNATIONAL PRESIDENT, RICHARD L. TRUMKA AND THE QUARTER OF A MILLION MEMBERS OF THE UNITED MINE WORKERS AND THEIR FAMILIES. I SPEAK, AS WELL, FOR TENS OF THOUSANDS OF WIDOWS AND OTHER DEPENDENTS WHO -- THOUGH NOT UMWA MEMBERS THEMSELVES -- ARE NONETHELESS BENEFICIARIES OF THE RETIREMENT BENEFITS EARNED BY THEIR DECEASED PARENTS AND SPOUSES FROM YEARS OF LABOR IN OUR NATION'S COAL MINES. I AM HERE TODAY AS THE LEGAL REPRESENTATIVE OF ALL UMWA MEMBERS -- WHETHER THEY BE ACTIVE OR LAID-OFF WORKERS OR RETIREES. WE APPRECIATE THE OPPORTUNITY TO ADDRESS, AND URGE YOUR SUPPORT FOR, THE RETIREE BENEFITS SECURITY ACT OF 1987.

BEFORE DETAILING OUR SUPPORT FOR SENATOR METZENBAUM AND HIS COLLEAGUES' INITIATIVE IN S. 548, I WOULD LIKE TO SHARE WITH YOU SOME INFORMATION ABOUT MINE WORKER RETIREES AND THEIR ROLE IN OUR UNION. THE PENSIONERS HOLD A SPECIAL PLACE IN THE UMWA. OUR UNION'S HISTORY HAS ITS ROOTS IN THE FAMILY TREES OF OUR MEMBERSHIP. MOST OF OUR ACTIVE MEMBERS ARE SECOND, THIRD AND FOURTH GENERATION COAL MINERS. THOSE WORKING MEMBERS ENTHUSIASTICALLY ACKNOWLEDGE THE DEBT THEY OWE TO THE RETIREES WHOSE COURAGE, SACRIFICE AND STEADFASTNESS BROUGHT DIGNITY, SECURITY AND A MEASURE OF SAFETY TO THE ARDUOUS AND DANGEROUS JOB OF MINING COAL. THROUGH THE EFFORTS OF THESE PAST GENERATIONS OF COAL MINERS, OUR MEMBERS HAVE BECOME ACTIVE PARTICIPANTS IN THE POLITICAL AND ECONOMIC DECISIONS THAT AFFECT THEIR LIVES.

IN RECOGNITION OF THE PROFOUND CONTRIBUTION MINE WORKER RETIREES HAVE MADE TO PRESENT-DAY ACTIVE COAL MINERS, OUR MEMBERS -- THROUGH DECADES OF COLLECTIVE BARGAINING -- HAVE MADE, AND CONTINUE TO MAINTAIN, RETIREES AS THE BENEFICIARIES OF THEIR LABOR. IN EXCHANGE FOR EACH HOUR THEY SPEND MINING COAL, UMWA COAL MINERS ARE PROMISED BY THEIR EMPLOYERS THAT A PORTION OF THE EXCHANGE VALUE OF THAT LABOR WILL GO TOWARDS MAINTAINING LIFETIME HEALTH BENEFITS FOR THOSE COAL MINERS WHO PRECEDED THEM -- INDIVIDUALS WHO USUALLY INCLUDE THEIR FATHERS AND GRANDFATHERS, UNCLES AND IN-LAWS.

MOREOVER, AND UNLIKE MOST LABOR ORGANIZATIONS, THE MINE WORKER CONSTITUTION PERMITS ACTIVE PARTICIPATION BY RETIREES IN THE INTERNAL GOVERNANCE OF OUR UNION. PENSIONERS SERVE AS DISTRICT AND LOCAL UNION OFFICERS. THEY PARTICIPATE AS REPRESENTATIVES ON THE COAL MINERS POLITICAL ACTION COMMITTEE AND HELP DETERMINE THE POLITICAL AND LEGISLATIVE AGENDA OF OUR ORGANIZATION. THEY SERVE AS DELEGATES TO INTERNATIONAL CONVENTIONS IN WHICH CAPACITY THEY PARTICIPATE DIRECTLY IN DECISIONS WHICH DETERMINE THE UNION'S FUTURE AND THE COLLECTIVE BARGAINING PRIORITIES FOR OUR NEGOTIATIONS TEAMS.

BECAUSE OF THIS SYMBIOTIC AND CONSTITUTIONAL RELATIONSHIP BETWEEN UMWA RETIREES AND WORKING MEMBERS, PENSIONER SECURITY IS A HALLOWED SUBJECT OF OUR AGREEMENTS. WHEN WE NEGOTIATE CONTRACTS WE ARE DIRECTED BY OUR MEMBERS, BOTH WORKING AND RETIRED, TO SECURE PROVISIONS GUARANTEEING HEALTH AND OTHER NON-PENSION BENEFITS FOR RETIRED COAL MINERS.

WHEN CONGRESS CHANGED THE BANKRUPTCY LAW IN 1984 TO ARREST THE UNILATERAL ABROGATION OF LABOR CONTRACTS BY CHAPTER 11 PETITIONERS, MY UNION SUPPORTED THESE PROVISIONS. WE FELT THEN ... AND NOW ... THAT THE PROVISIONS OF SECTION 1113 OF THE ACT PROHIBITED THE UNILATERAL REJECTION OF ANY PROVISION MAINTAINED

OR ESTABLISHED BY COLLECTIVE BARGAINING AGREEMENTS, INCLUDING RETIREE BENEFITS SUCH AS HEALTH INSURANCE. SOME BANKRUPTCY COURTS, HOWEVER, APPARENTLY DO NOT SHARE OUR READING OF THE STATUTE, DESPITE THE FACT THAT SUBSECTION F OF SECTION 1113 PROVIDES -- IN CRYSTAL CLEAR TERMS -- THAT A TRUSTEE OR DEBTOR-IN-POSSESSION SHALL NOT BE PERMITTED TO UNILATERALLY TERMINATE OR ALTER ANY PROVISION OF A COLLECTIVE BARGAINING AGREEMENT.

DECISIVE LEGISLATION, SUCH AS SECTION 2(a) OF S. 548, CLARIFYING AND FORMALIZING CONGRESS' INTENT IN THIS REGARD IS URGENTLY NEEDED, AND HAS OUR UNION'S FULL SUPPORT.

THE COLLECTIVE BARGAINING AGREEMENTS UNDER WHICH OUR MEMBERS HAVE MINED COAL SINCE 1947 REQUIRE THAT EACH SIGNATORY EMPLOYER ESTABLISH AND MAINTAIN BENEFIT PLANS TO PROVIDE HEALTH AND OTHER NON-PENSION BENEFITS TO RETIREES. DURING THE TERM OF THOSE AGREEMENTS, OUR ACTIVE MEMBERS HAVE DERIVED SECURITY FROM KNOWING TWO THINGS: FIRST, HIS OR HER FELLOW UNION MEMBERS WHO ARE RETIREES WILL CONTINUE TO RECEIVE LIFETIME HEALTH BENEFITS; AND, SECOND, SUCH BENEFITS WILL BE PROVIDED THEM WHEN THEY RETIRE FROM ACTIVE SERVICE. THESE ARE, OF COURSE, VERY POWERFUL INDUCEMENTS TO KEEP A COAL MINER ON A JOB WHEREIN THE THREAT OF INJURY AND OCCUPATIONAL DISEASE GROWS MORE MENACING AS HIS AGE ADVANCES.

WE NOTE THAT THE SECOND CIRCUIT COURT OF APPEALS HAS ENDORSED OUR READING OF SECTION 1113. IN *IN RE CENTURY BRASS PRODUCTS, INC*., 795 F.2d 265 (1986), THAT COURT RULED THAT RETIREE BENEFITS PROVIDED UNDER A COLLECTIVE BARGAINING AGREEMENT MAY NOT BE UNILATERALLY REJECTED AND ARE SUBJECT TO MODIFICATION ONLY IF SECTION 1113 PROCEDURES ARE FOLLOWED. THE COURT HELD THAT RETIREES ARE PROPERLY CHARACTERIZED AS EMPLOYEES FOR PURPOSES OF SECTION 1113 AND THAT THEY ARE

GENERALLY CAPABLE OF BEING REPRESENTED BY THEIR UNION IN THE NEGOTIATIONS REQUIRED UNDER THAT PROVISION.

HOWEVER, WHEN THE LTV COMPANIES FILED FOR CHAPTER 11 PROTECTION LAST JULY, THAT COMPANY UNILATERALLY TERMINATED ITS RETIREES' HEALTH AND LIFE INSURANCE BENEFITS. THE BANKRUPTCY COURT WITH RESPONSIBILITY FOR THE FILING DID NOT SWIFTLY DECLARE SUCH ACTION ILLEGAL UNDER SECTION 1113 AS AN UNAUTHORIZED BREACH OF THE COMPANY'S COLLECTIVE BARGAINING AGREEMENT. BUT FOR THE RESOLUTE AND PROMPT RESPONSE OF BOTH HOUSES OF CONGRESS COMPELLING THE DEBTOR TO RESUME PAYING RETIREE BENEFITS TO TENS OF THOUSANDS OF RETIRED STEELWORKERS, AUTO WORKERS AND MINE WORKERS, AGREEMENTS MADE THROUGH DECADES OF FREE COLLECTIVE BARGAINING IN THREE CRITICAL AMERICAN INDUSTRIES COULD HAVE BEEN NULLIFIED BY UNILATERAL ACTION -- THE ANTITHESIS OF LABOR RELATIONS CONTRACT FORMATION.

LET US NOT FORGET, THOUGH, THE CONCERTED ACTION OF STEELWORKERS WHO WENT ON STRIKE AT LTV'S HARBOR WORKS IN EAST CHICAGO, INDIANA BECAUSE THEY CONSIDERED THE COMPANY'S CANCELLATION OF RETIREE BENEFITS AN INEXPIABLE BREACH OF THE CONTRACT UNDER WHICH THEY LABOR. THE COLLECTIVE ACTION OF THESE STEELWORKERS HAMMERS HOME A SALIENT FEATURE OF THE TERMS UNDER WHICH THEY -- AND THE MINE WORKERS -- BARGAIN CONTRACTS AND WORK. AT THE DIRECTION OF OUR WORKING MEMBERS, WE HAVE CHOSEN TO ASSIGN TO RETIREES A PORTION OF THE ECONOMIC VALUE WE RECEIVE IN EXCHANGE FOR OUR LABOR. WE DO THIS, SOMETIMES, IN LIEU OF HIGHER WAGES. WHEN LTV REJECTED THE RETIREMENT BENEFITS OF ITS PENSIONERS, THE STEELWORKERS SET DOWN THEIR TOOLS, FOR THEY CONSIDERED THE COMPANY'S ACTIONS TO BE A BREACH OF THE TERMS OF THEIR AGREEMENT. I ASSURE YOU THAT IS NO LESS THE CASE IN THE AMERICAN COAL FIELDS.

IN ADDITION, FOR THE REASONS SET FORTH BELOW, WE

PARTICULARLY APPLAUD THE PROVISIONS OF S. 548 WHICH CLASSIFY POST-PETITION PAYMENTS OF RETIREE BENEFITS AS ADMINISTRATIVE EXPENSES. THESE PROVISIONS ALSO PRECLUDE SET-OFFS FOR BENEFITS PAID POST-PETITION -- BUT PRIOR TO A REORGANIZATION PLAN'S CONFIRMATION -- FROM UNPAID FUTURE BENEFITS, UNLESS SUCH A SET-OFF IS AGREED TO BY THE DEBTOR AND THE AUTHORIZED REPRESENTATIVE OF THE RETIREES.

UMWA RETIREES' HEALTH BENEFITS ARE PART OF OUR COLLECTIVE BARGAINING AGREEMENT AND OUR MEMBERS FEEL STRONGLY THEY BE ACCORDED THE SAME LEGAL STATUS THAT THE BANKRUPTCY ACT CONFERS UPON OTHER COLLECTIVELY-BARGAINED BENEFITS. IN THE WORDS OF ONE COURT,

> "IT IS NOT NECESSARY TO DISCUSS THE ECONOMIC BENEFIT CONTRIBUTED BY THE PENSIONERS OR TO DETERMINE ITS PRESENT STATUS, SINCE HERE THE EXPRESS LANGUAGE OF THE LABOR CONTRACT MAKES THE PAYMENT OF PENSIONS A PART OF THE CONSIDERATION FOR THE DAY TO DAY EFFORTS OF THE EMPLOYEES. THE HOURLY RATE OF PAY, THE PROVISION FOR VACATION PAY, SENIORITY RIGHTS, THE SETTLEMENT OF GRIEVANCES, ARE ALL A PART OF THE BENEFITS RECEIVED BY THE WORKER. THEY ARE A PART OF THE REWARD FOR HIS EFFORT; A PART OF HIS WAGE ... AND THIS COURT IS NOT JUSTIFIED IN ATTEMPTING TO SEPARATE OR ISOLATE THE ELEMENTS WHICH GO TO MAKE UP THE TOTAL BENEFITS. THEY ARE ALL IN ONE PACKAGE." IN RE SCHENECTADY RY. CO., 93 F.Supp. 67, 70 (S.D.N.Y. 1950).

OPPONENTS OF S. 548 WILL COUNSEL OUR PENSIONERS TO TAKE THEIR PLACE IN LINE WITH OTHER CREDITORS, SECURED AND

UNSECURED, OF THE BANKRUPT COMPANY. THEY WILL TELL YOU THAT THE RETIREES CLAIMS SHOULD BE ACCORDED NO MORE PRIORITY THAN ANY OTHER PRE-PETITION CLAIM, PROFESSING THAT THEY ARISE OUT OF A PRE-PETITION AGREEMENT AND WERE EARNED WHOLLY DURING THE PRE-PETITION PERIOD. SUCH A VIEW MISPERCEIVES, WE FEEL, THE FUNDAMENTAL NATURE OF THE LABOR WHICH IS PERFORMED BY EMPLOYEES DURING THE POST-PETITION PERIOD. IT IGNORES THE INDISPUTABLE FACT THAT RETIREE HEALTH BENEFITS ARE PART AND PARCEL OF THE QUID PRO QUO FOR THE LABOR A DEBTOR'S EMPLOYEES PROVIDE AFTER A PETITION HAS BEEN FILED.

RETIREES SHOULD ASSUME THE SAME STATUS AS OTHER PARTIES WILLING TO PROVIDE THOSE SERVICES NECESSARY TO KEEP THE COMPANY AFLOAT, PROTECT ITS ASSETS, AND PREVENT LIQUIDATION -- ALL TO THE BENEFIT OF THE COMPANY'S CREDITORS. THE DEBTOR-IN-POSSESSION IS A SEPARATE LEGAL ENTITY THAT IS CARRYING ON ITS BUSINESS PRINCIPALLY ON BEHALF OF THE PRE-FILING CREDITORS. WHEN A DEBTOR'S EMPLOYEES ARE INDUCED TO CONTINUE SUPPLYING THEIR SERVICES, THE LAW SHOULD CLEARLY REQUIRES THAT THEIR REMUNERATION BE ACCORDED THE STATUS OF ADMINISTRATIVE COSTS; FOR ANY CLAIMS INCIDENT TO THE DEBTOR-IN-POSSESSION'S CONTINUED OPERATION OF THE BUSINESS -- SUCH AS THOSE OF THE EMPLOYEES WHOSE VERY LABOR IS MAKING REORGANIZATION POSSIBLE -- MUST BE PAID BEFORE THE CLAIMS OF THE CREDITORS FOR WHOSE BENEFIT THE CONTINUED OPERATION OF THE BUSINESS IS BEING CONDUCTED.

IN BILDISCO THE SUPREME COURT STATED THAT A DEBTOR-IN-POSSESION WHO ELECTS TO CONTINUE TO RECEIVE BENEFITS FROM ITS EMPLOYEES IS OBLIGATED TO PAY THE REASONABLE VALUE OF THOSE SERVICES. SEE NLRB v. BIDLISCO & BILDISCO, 465 U.S. 513, 531 (1984). THE COURT OBSERVED THAT A REASONABLE RETURN MAY VERY WELL BE WHAT IS SPECIFIED IN THE COLLECTIVE BARGAINING AGREEMENT. FOLLOWING BILDISCO THE UMWA SUBMITS THAT THE TERMS

AND CONDITIONS OF A COLLECTIVE BARGAINING AGREEMENT MUST BE MET -- AT LEAST UNTIL A SECTION 1113 DECISION IS ISSUED -- IF THE DEBTOR TAKES ADVANTAGE OF POST-PETITION LABOR PERFORMED BY ITS EMPLOYEES. THUS, UNTIL A PLAN MODIFYING THE TERMS AND CONDITIONS OF A COLLECTIVE BARGAINING AGREEMENT IS CONFIRMED, THE EMPLOYEES' SERVICES SHOULD PROPERLY BE DEEMED ADMINISTRATIVE EXPENSES. WITHOUT THEIR LABOR THE CONTINUED OPERATION OF THE COMPANY WOULD NOT BE POSSIBLE AND REORGANIZATION WOULD LIKELY BE UNSUCCESSFUL. WHERE THE LABOR CONTRACT REQUIRES A RETIREE HEALTH AND WELFARE PLAN, THE RETIREE BENEFITS MUST BE MAINTAINED.

IN ADDITION, WE NOTE AS WELL THE FACT THAT COURTS HAVE AFFORDED PROTECTION TO RETIREE BENEFITS ARISING OUT OF EXPIRED COLLECTIVE BARGAINING AGREEMENTS. THROUGH SUCCESSIVE AGREEMENTS, THE COAL COMPANIES FOR WHOM OUR RETIRED MEMBERS MINED COAL OFFERED THEM A FUTURE OF HEALTH AND OTHER RETIREMENT BENEFITS IN EXCHANGE FOR THEIR PROMISE TO PROVIDE LABOR TO THOSE EMPLOYERS. OUR COURTS HAVE DETERMINED THAT SUCH AGREEMENTS CREATE VALID AND ENFORCEABLE CONTRACT RIGHTS UNDER FEDERAL LAW. AN EMPLOYER'S OFFER OF RETIREMENT BENEFITS BECOMES AN IRREVOCABLE OBLIGATION UPON THE EMPLOYEE'S PERFORMANCE OF THE REQUIRED SERVICE. SEE, E.G., ROCHESTER CORPORATION v. ROCHESTER, 450 F.2d 118, 120-21 (4TH CIR. 1971); HOEFEL v. ATLAS TACK CORPORATION, 581 F.2d 1, 4-5 (1ST CIR. 1977) AND IN RE ERIE LACKAWANNA RAILWAY COMPANY, 548 F.2d 621 (6TH CIR. 1977). CASE LAW PROVIDES THAT WHERE AN EMPLOYEE HAS COMPLIED WITH THE CONDITIONS OF A COLLECTIVE BARGAINING AGREEMENT CONTAINING PROMISES OF BENEFITS INDUCING HIM TO CONTINUE HIS SERVICE TO THE EMPLOYER, THAT EMPLOYEE ACQUIRES, AT RETIREMENT AGE, A VESTED RIGHT TO THE THOSE BENEFITS. SUCH "STATUS" BENEFITS ARE TO CONTINUE SO LONG AS THE PREREQUISITE STATUS IS MAINTAINED. WHERE CONTRACTED FOR RETIREMENT BENEFITS ACCRUE UPON THE ACHIEVEMENT OF RETIREE STATUS, THEN THOSE

BENEFITS ARE TO CONTINUE AS LONG AS THE BENEFICIARY REMAINS A RETIREE, NOTWITHSTANDING THE FACT THE COLLECTIVE BARGAINING AGREEMENT HAS EXPIRED. SEE, E.G., INTERNATIONAL UNION, UNITED AUTOMOBILE, AEROSPACE & AGRICULTURAL IMPLEMENT WORKERS v. YARD-MAN, INC., 716 F.2d 1476, 1482 n. 8 (6TH CIR. 1983); POLICY v. POWELL PRESSED STEEL, 770 F.2d 609, 612-13 (6TH CIR. 1985); WEIMER v. KURZ-KASCH, INC., 773 F.2d 669, 672-73 (6TH CIR. 1985).

WHEN SENATOR METZENBAUM INTRODUCED S. 548 HE COMMENTED THAT CONGRESS ANTICIPATED THAT SECTION 1113 WOULD PROTECT ALL PORTIONS OF A UNION'S COLLECTIVE BARGAINING AGREEMENT FROM UNILATERAL REJECTION. INDEED, IF REJECTIONS OF RETIREE BENEFITS CONTINUE UNABATED, AMERICAN WORKERS WILL AGAIN FACE THE KIND OF INSIDIOUS THREATS TO THEIR SECURITY THAT THE 1984 AMENDMENTS SOUGHT TO ELIMINATE. THE 1984 ACT WAS PASSED, IN PART, IN RESPONSE TO ALLEGATIONS THAT UNSCRUPULOUS EMPLOYERS WERE USING THE THREAT OF BANKRUPTCY TO FORCE WORKERS INTO ACCEPTING CONCESSIONS IN WAGES AND WORKINGS CONDITIONS. NOW THE THREATS TAKE A NEW, AND EQUALLY TREACHEROUS FORM: THIS TIME, HOWEVER, RETIREES ARE THE HOSTAGES. WORKERS ARE FORCED TO EITHER ACCEPT THE CONCESSIONS DEMANDED BY THEIR EMPLOYER OR SEE THEIR PARENTS' AND GRANDPARENTS' FIXED INCOMES RAVAGED BY SKYROCKETING MEDICAL COSTS.

FINALLY, THE UMWA WHOLEHEARTEDLY SUPPORTS SECTION 2(b) OF S. 548, WHICH SPECIFIES THAT CLAIMS ARISING UNDER ANY COLLECTIVE BARGAINING AGREEMENT, INCLUDING ANY CLAIM RELATING TO BENEFITS FOR RETIRED EMPLOYEES, SHALL NOT BE SUBJECT TO THE LIMITS OF SECTION 502(b)(7) OF THE BANKRUPTCY CODE. AS THE UNITED AUTO WORKERS NOTE IN THEIR TESTIMONY, SECTION 502(b)(7) WAS NEVER INTENDED TO LIMIT THE CLAIMS ARISING UNDER COLLECTIVE BARGAINING AGREEMENTS. INDEED, THAT PART OF THE LAW APPLIES EXPLICITLY TO EMPLOYMENT CONTRACTS, NOT TO COLLECTIVE

BARGAINING AGREEMENTS. THE DISTINCTION BETWEEN THE TWO HAS BEEN LONG RECOGNIZED. IN J. I. CASE v. NLRB, THE SUPREME COURT NOTED,

> "COLLECTIVE BARGAINING BETWEEN EMPLOYER AND THE REPRESENTATIVE OF A UNIT, USUALLY A UNION, RESULTS IN AN ACCORD AS TO TERMS WHICH WILL GOVERN HIRING AND WORK AND PAY IN THAT UNIT. THE RESULT IS NOT, HOWEVER, A CONTRACT OF EMPLOYMENT EXCEPT IN RARE CASES; NO ONE HAS A JOB BY REASON OF IT AND NO OBLIGATION TO ANY INDIVIDUAL ORDINARILY COMES INTO EXISTENCE FROM IT ALONE. THE NEGOTIATIONS BETWEEN UNION AND MANAGEMENT RESULT IN WHAT OFTEN HAS BEEN CALLED A TRADE AGREEMENT, RATHER THAN A CONTRACT OF EMPLOYMENT." 321 U.S. 332, 334-35.

SEE ALSO HENDRICKS v. AIRLINE PILOTS ASSOCIATION, INTERNATIONAL, 696 F.2d 673, 676 (9TH CIR. 1983). CLEARLY, IF EMPLOYEES WORKING UNDER A COLLECTIVE BARGAINING AGREEMENT CANNOT AVAIL THEMSELVES OF GENERAL CONTRACT REMEDIES, SUCH AS PERFORMANCE OF THE CONTRACT, THEN THEY CANNOT BE HELD TO LIMITATIONS THE LAWS PLACE ON EMPLOYMENT CONTRACTS.

* * * * *

IN PASSING SECTION 1113, CONGRESS HAS MANIFESTLY DEMONSTRATED AN OVERRIDING CONCERN FOR THE EQUITIES IN BANKRUPTCY PROCEEDINGS. INDEED, THE BANKRUPTCY COURTS SIT IN EQUITY, MATTER OF STERLING HOMEX CORP., 591 F.2d 148 (2D CIR. 1978), 11 U.S.C. § 205, AND IN THAT CAPACITY MUST BE DIRECTED, AS THIS BILL PROPOSES, TO GIVE DUE CONSIDERATION TO THE PROFOUND HARDSHIP THE BANKRUPTCY LAW NOW UNWITTINGLY IMPOSES UPON THE VERY PEOPLE LEAST ABLE TO REBOUND FROM THEIR EMPLOYERS' FINANCIAL COLLAPSE. WHILE YOUNGER WORKERS MAY

HARBOR THE HOPE -- HOWEVER UNREALISTIC IT MAY BE IN THE PRESENT ECONOMIC CLIMATE -- OF FINDING OTHER REMUNERATIVE WORK AND ULTIMATELY REESTABLISHING FINANCIAL FOOTING, OUR RETIREES DO NOT HAVE THE LUXURY OF YOUTH AND ITS ATTENDANT OPPORTUNITY. IT IS UNREALISTIC TO PROJECT THAT RETIREES, MOST OF WHOM SUBSIST ON LOW FIXED INCOMES, WILL SOME DAY FIND SOME OTHER SOURCE OF MEDICAL COVERAGE. THE UNITED MINE WORKERS OF AMERICA URGES THE CONGRESS TO TAKE QUICK REMEDIAL ACTION. IF HOW WE TREAT OUR SENIOR CITIZENS IS A MEASURE OF OUR COMPASSION, IT IS A MEASURE OF OUR HUMANITY TO SEE HOW WE TREAT THOSE UPON WHOSE LABOR OUR SOCIETY AND OUR NATION WAS BUILT.

THANK YOU.

United Mine Workers of America

MICHAEL H. HOLLAND
GENERAL COUNSEL

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UNITED MINE WORKERS' BUILDING
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20005

May 6, 1987

HAND-DELIVERED

Senator Howell Heflin
Chairman, Subcommittee on Courts and
Administrative Practice
United States Senate Committee
on the Judiciary
Washington, DC 20510

Dear Senator Heflin:

Enclosed please find my answers, on behalf of the UMWA, to the supplemental questions submitted by members of the Subcommittee following the April 1, 1987, hearing on the Retiree Benefits Security Act. I apologize for the delay in returning these responses; I have spent the last several weeks in the Western states engaged in collective bargaining negotiations. I hope that my answers are sufficiently timely to be included in the hearing record.

Finally, I want to thank you for extending the UMWA the opportunity to testify in support of the Retiree Benefits Security Act. I hope you and your fellow Committee members find my testimony, as well as the additional comments supplied herewith, to be useful and informative.

Very truly yours,

Michael Holland

cc: Richard L. Trumka, International President
Cecil E. Roberts, International Vice President
John J. Banovic, International Secretary-Treasurer
Bill Banig, Deputy Director, COMPAC

Questions for Michael Holland, United Mine Workers of America

1. WHERE THERE ARE UNION EMPLOYEES AND NON-UNION EMPLOYEES OF THE SAME COMPANY, DOES S. 548 COMTEMPLATE THAT THERE WILL BE TWO SEPARATE CREDITORS "COMMITTEES"? IF SO, WOULD EACH HAVE TO GO THROUGH THE PROPOSED MODIFICATIONS SEPARATELY?

A union is required to bargain on behalf of all bargaining unit employees, irrespective of their union membership. Accordingly, union employees and non-union employees would be identically situated under S. 548. Their rights to retiree benefits would arise from the same collective bargaining agreements and under proposed sections 1113(h) and (i), the union and non-union retirees would share the same authorized representative -- just as they do now under our national labor laws.

2. COULD THERE BE A SITUATION WHERE RETIREMENT BENEFITS COULD BE MODIFIED FOR ONE TYPE OF RETIRED EMPLOYEE BUT NOT FOR OTHERS, BASED ON WHETHER YOU WERE IN A UNION?

No, not if the employees were working under the same collective bargaining agreement.

3. ARE THERE ANY PROVISIONS IN S. 548 FOR THE PAYMENT OF RETIREMENT BENEFITS TO MANAGEMENT?

Absolutely. Section 1114, subsections (b), et seq., cover recipients of retiree benefits not covered by a collective bargaining agreement.

4. WHO PAYS FOR LEGAL COUNSEL TO REPRESENT THE INTERESTS OF VARIOUS COMMITTEES? ARE COUNSEL PAID OUT OF PAYMENTS THAT WOULD OTHERWISE BE DISTRIBUTED TO RETIREES?

The law does not address this question. Of course, when the UMWA is the authorized representative of the retirees, the Union will provide the necessary legal services.

QUESTIONS FOR THE UNION PANELS

1. S. 548 WOULD AMEND SECTION 1113(f) BY ADDING THE LANGUAGE "INCLUDING ANY PROVISION RELATING TO BENEFITS FOR RETIRED EMPLOYEES." WOULD THIS LANGUAGE INCLUDE PENSION BENEFITS? IS THIS NOT IN CONFLICT WITH THE LEGISLATION PASSED AS A PART OF THE RECONCILIATION BILL LAST YEAR WHICH PROVIDED THAT TO TERMINATE PENSION BENEFITS, A COMPANY HAD TO COMPLY WITH THE ERISA LAWS? DOES THIS NOT SEVERELY IMPACT UPON A COMPANY'S ABILITY TO REORGANIZE?

The language added to Section 1113(f) by S. 548 clarifies that Section 1113(f) -- even as presently written -- protects all collectively bargained benefits from unilateral modification or termination by a Chapter 11 entity. Thus, if pension benefits are provided under a collective bargaining agreement, then pension benefits fall under the statute's protections. The proposed language is not in conflict with legislation passed as part of the reconciliation bill last year. The proposed amendments to S. 548 govern an employer's obligations under a collective bargaining agreement to maintain benefit levels specified in the collective bargaining agreement until or unless relief is granted under a plan of reorganization. The ERISA laws could, in reality, protect only a portion of the pension benefits provided under the collective bargaining agreement. The minimum benefit levels guaranteed by ERISA may fall well below benefits contained in the plan. This is particularly true for surviving spouse benefits. Moreover, ERISA does not guarantee all benefit types. Finally, as the LTV bankruptcy has demonstrated, there could be a significant lag time between an employer's suspension of pension benefits and PBGC action. Elderly people on fixed incomes face severe hardship if their pensions are cut off for even one month. Accordingly, the section 1113(f) prohibition against unilateral rejection of contractual pension benefits ensures that reorganization is accomplished in a manner which is equitable and does not unfairly burden retirees.

2. THE LANGUAGE OF PROPOSED SECTION 1113(g) EXEMPTS ALL CLAIMS ARISING UNDER ANY COLLECTIVE BARGAINING AGREEMENT COVERED BY SECTION 1113 FROM THE ONE-YEAR LIMIT IN DAMAGES IN SECTION 502(b)(7). DOES THIS EXEMPTION FROM 502(b)(7) EXTEND ONLY TO CLAIMS INVOLVING MEDICAL AND INSURED BENEFITS, OR IS THE LANGUAGE ALL INCLUSIVE? IS THE STANDARD THE SAME FOR UNION AND NON-UNION EMPLOYEES? RETIRED AND CURRENT EMPLOYEES?

As I stated in my testimony, all claims arising under any collective bargaining agreement are exempt from the one-year limit in damages contained in Section 502(b)(7) because the latter provision applies expressly to employment contracts, and not to collective bargaining agreements. Proposed section 1114(i) would accord similar protection to retiree benefits of employees who are not covered by a collective bargaining agreement.

**3. WHAT POLICY CONSIDERATIONS DICTATE ESTABLISHING RETIREES AS A SEPARATE CLASS FOR PURPOSES OF VOTING ON A PLAN OF REORGANIZATION, AND HOW WILL THIS AFFECT THE RIGHTS OF OTHER UNSECURED CREDITORS?**

Retirees share a unique community of interests which justifies establishing them as a separate class for purposes of voting on a plan of reorganization. Retirees' health, welfare and security is best preserved if the retirees possess a unified voice in plan confirmation proceedings. Placing retirees in the same class as creditors whose personal health and welfare will not be affected by the final reorganization plan, may compromise the Court's ability to make a ruling on the fairness and equity of the plan with respect to elderly creditors whose lives lie in the balance. Section 1129 of the Code, as amended, would permit the Court to overrule any objections posed by the retiree class so long as the plan is fair, equitable and nondiscriminatory with respect to each class of claims and interests. The rights of other unsecured creditors will be affected only to the extent that they must share the burdens of reorganization that might otherwise fall disproportionately upon the class least able to absorb the hardship -- the elderly.

**4. IF THE RECOGNIZED EXCLUSIVE COLLECTIVE BARGAINING REPRESENTATIVE OF THE EMPLOYEES ELECTS NOT TO SERVE AS THE AUTHORIZED REPRESENTATIVE, THE COURT SHALL APPOINT A COMMITTEE OF RETIREE EMPLOYEES.**

**a. IF A COMPANY HAS RETIRED WORKERS WHO ARE COVERED BY A COLLECTIVE BARGAINING AGREEMENT, AND WORKERS WHO ARE NOT COVERED BY A COLLECTIVE BARGAINING AGREEMENT, WOULD THIS LEGISLATION ESTABLISH TWO SEPARATE COMMITTEES OF RETIRED EMPLOYEES?**

**b. HOW LARGE WILL THIS COMMITTEE BE IN TERMS OF PROVIDING REPRESENTATION FOR THE RETIRED WORKERS?**

**c. WILL THE COMMITTEE BE AUTHORIZED TO HIRE ATTORNEYS AS OTHER UNSECURED CREDITORS COMMITTEE ARE ALLOWED TO DO? WHAT ARE ALL THE POWERS OF THE RETIREES COMMITTEE?**

a. The Court might determine, at its discretion, that the two groups of workers could be adequately represented by the same authorized representative. The Court might also, at its discretion, appoint a separate committee to act as authorized representative of those employees not covered by a collective bargaining agreement.

b. The size of the committee to act as representative for the retired workers is left to the discretion of the Court.

c. The bill does not state whether the committee acting as authorized representative of retirees is authorized to hire attorneys as other unsecured creditor committees are permitted to do. The retirees committees have the power, granted under §§ 1113 and 1114, to seek enforcement of retirees rights under procedures provided in the aforesaid provisions. The committee acting as authorized representative for a group retirees is enpowered to initiate such legal actions as may be necessary to ensure compliance with the terms of the reorganization plan.

**5. IT IS MY UNDERSTANDING THAT THE POWER TO REJECT A COLLECTIVE BARGAINING AGAREEMENT UNDER SECTION 1113 OF TITLE 11 OF THE CODE DOES NOT CARRY WITH IT A CORRESPONDING POWER OF MODIFYING THE AGREEMENT AS REJECTED, LEAVING THE PARTIES FREE TO RENEGOTIATE. THIS BILL SEEMS TO CHANGE THAT POLICY BY ALLOWING FOR MODIFICATION (Sections 1114(e) AND (f)), BUT REQUIRING THE COURT, AT THE SAME TIME, NOT TO SET THE LEVEL BELOW THAT RECOMMENDED TO ALLOW THE COMPANY TO CONTINUE IN BUSINESS AND THAT WHICH IS FAIR AND EQUITABLE TO ALL PARTIES.**

S. 548 gives the Court greater latitude than does Section 1113 as currently written and provides some critical clarity to the provision. The case law on § 1113 is in the process of developing. Under that current provision, I understand that many bankruptcy lawyer argue that a Court may only either approve or not approve an application for rejection or modification of a collective bargaining agreement filed by the debtor-in-possession or trustee. Under the proposed amendment, however, it is clear that the Court may impose such modifications to retiree benefits as the Court deems necessary to permit reorganization of the debtor while treating all parties fairly and equitably. Under present Section 1113 the debtor-in-possession or trustee is required to meet and confer in good faith with the collective bargaining representative of the employees in attempting to reach mutually satisfactory modifications to the collective bargaining agreement. If retiree benefits obligations arise out of the collective bargaining agreement then, naturally, they are subject to renegotiation by the parties under the aforesaid procedures.

**6. S. 548 REQUIRES EMPLOYERS TO PAY RETIREE INSURANCE BENEFITS AS AN EXPENSE OF ADMINISTRATION. I HAVE TWO QUESTIONS:**

**a. WILL THIS CREATE SUCH A BURDEN ON THE DEBTOR COMPANY THAT IT WILL PREVENT REORGANIZATION UNDER CHAPTER 11.**

**b.. WHY IS IT NECESSARY TO PROVIDE THESE EXPENSES AS ADMINISTRATIVE EXPENSES?**

a. As I stated in my testimony, UMWA members mine coal under collective bargaining agreements which contain provisions detailing contributions which employers must make to retiree benefit plans. To the extent they are a labor cost during the post-petition period, retiree insurance benefits premiums are an expense of administration, for they are among the costs of keeping the company afloat. With respect to those retiree benefits which do not arise out of a collective bargaining agreement, designating them administrative expenses is a necessary consequence of the law's requirement that the benefits not be modified or terminated until such changes are approved by an order of the Court. This should not burden the debtor companies so as to prevent reorganization under Chapter 11 because Section 1114(g) contains allowances for interim relief where irreparable damage to the estate is established.

**7. IF THESE BENEFIT PAYMENTS ARE TREATED AS ADMINISTRATIVE EXPENSES, WHY IS IT NECESSARY TO ESTABLISH RETIRED WORKERS AS A SEPARATE CLASS FOR PURPOSES OF CONFIRMING A PLAN OF REORGANIZATION UNDER SECTION 1129?**

The benefit payments' status as administrative expenses only protects the benefits from modification or termination until such time as a plan is confirmed under Section 1129. The terms and conditions of the subsequent plan, will affect the level of benefits of retirees as a class.

8. WHAT IS THE EFFECT AND PURPOSE OF SECTION 1114(h) OF THIS LEGISLATION WHICH WOULD PREVENT THE DEBTOR FROM OFFSETTING PAYMENTS OF HEALTH AND MEDICAL BENEFITS MADE DURING THE TIME OF FILING OF THE PETITION AND COMFIRMATION FROM PAYMENTS THAT WILL BE PAID AS PART OF THE PLAN OF REORGANIZATION?

For benefits that are paid pursuant to a collective bargaining agreement, it is merely recognition that those benefit payments are part of the administrative expense of continuing in business during the post-petition period and prior to confirmation of the plan of reorganization. With respect to all other benefits, Section 1114(h) recognizes that the level of benefits provided under the plan of reorganization is determined after a searching inquiry into fairness and equity. If the offsetting of payments were permitted, this would cause benefits to fall below those levels which the Court has determined are necessary in order to save retirees from undue hardship and burden.

## QUESTIONS FOR UNION PANEL BY SENATOR THURMOND

1. I FEEL THAT ANY LEGISLATION WHICH THE CONGRESS PASSES MUST INSURE THAT UNION AND NON-UNION RETIREES ARE TREATED EXACTLY THE SAME IN CHAPTER 11 PROCEEDINGS. DO YOU BELIEVE THAT S. 548, AS CURRENTLY DRAFTED, INSURES THAT RESULT?

Yes, with respect to retiree benefits, they are treated the same. Insofar as pension benefits are provided under a collective bargaining agreement, S. 548 clarifies that such benefits may not, under 1113, be unilaterally modified or terminated. That pensions of non-union employees are not similarly protected is part of the reality that benefits of non-union employees are always vulnerable to unilateral modification by employers.

**2. THIS LEGISLATION ALLOWS THE LABOR ORGANIZATION WHICH REPRESENTS EMPLOYEES COVERED BY A COLLECTIVE BARGAINING AGREEMENT TO CHOOSE TO BECOME THE AUTHORIZED REPRESENTATIVE OF THOSE RETIREES RECEIVING BENEFITS COVERED BY THAT AGREEMENT. GIVEN THAT THE INTEREST OF CURRENT EMPLOYEES AND RETIREES ARE HARDLY IDENTICAL, DOES NOT THIS PROVISION OF THE LEGISLATION CREATE A POTENTIAL CONFLICT OF INTEREST FOR THE LABOR ORGANIZATION IF IT ELECTS TO BECOME THE AUTHORIZED REPRESENTATIVE?**

As I stated in my initial testimony, such a conflict of interest does not exist in the United Mine Workers of America. I will add, however, that there are always conflicts within membership organizations. The democratic processes through which unions conduct self-governance, however, are adequate for resolving such conflicts. I also believe that the resources and expertise available to a labor union will make it a most effective representative of retirees in Chapter 11 proceedings.

Senator HEFLIN. I will submit my questions in writing.

Senator Metzenbaum.

Senator METZENBAUM. I have just a couple short ones. I would ask Mr. Nicholson, has the UAW faced retiree health terminations at other companies?

Mr. NICHOLSON. Yes. One situation I mentioned was Allis Chalmers Corporation where the Wall Street Journal recently reported that they were saying they may file chapter 11 unless they can get substantial reductions in their retiree insurance benefits. There are thousands of Allis Chalmers retirees, and there are other companies as well.

Senator METZENBAUM. Under current law, if a bankruptcy court terminates a collective bargaining agreement, what happens to retiree health benefits? And are you satisfied the bill adequately addresses this problem?

Mr. NICHOLSON. Well, first of all, for nonunion retirees, the current law offers them no protection, and we are aware of several situations, in addition to LTV, where nonunion retirees have been totally cut off.

With respect to union retirees having benefits under a collective bargaining agreement, section 1113, as currently in force, provides that as a prerequisite to a court ordering rejection, the court must find that the debtor made a proposal for necessary modifications in the agreement. But once the court enters an order, it enters an order rejecting the agreement; it does not enter an order per se ordering modification of the contract. And there are situations out there where employers postrejection have taken the position that, as with other executory contracts, once a contract is rejected, a labor agreement, there is no obligation that arises under that agreement that is enforceable. And in those situations, employers have argued and, in fact, actually cut off all retiree benefits, even if they could afford to pay some and even though they may have proposed to continue to pay some under their prerejection proposal.

So, clearly, the legislation needs to address that, and this bill does by providing that after rejection, the retiree benefits have to continue for union retirees at a level that meets the necessity and equity standards in this legislation.

Senator **Metzenbaum**. Thank you very much.

Mr. Holland, I do have a couple questions for you, but I am going to submit them to you in writing. I hope you will respond promptly.

Mr. **Holland**. I will be pleased to. Thank you, Senator.

Senator **Metzenbaum**. Thank you, Mr. Chairman.

Senator **Heflin**. To all staff people who would like for their Senators to submit questions, the questions have to be submitted and mailed to these gentlemen here, as well as the others that have testified, by April 8, and the answers returned by April 20.

Thank you, gentlemen, we appreciate your testimony.

We will now hear from our retiree panel: Mr. Grayson Kirtland, A.H. Robins retired employee; Mrs. Lillian Lemmens, who is a widow of an LTV worker from Strongville, OH; and Mrs. Kathryn O. Hunt, the wife of an LTV employee from Cleveland, OH.

If you will come forward, we will be delighted. First on my list is Mr. Kirtland.

## STATEMENTS OF A PANEL CONSISTING OF GRAYSON KIRTLAND, RETIRED EMPLOYEE, A.H. ROBINS CO.; LILLIAN LEMMENS, STRONGVILLE, OH; AND KATHRYN O. HUNT, CLEVELAND, OH

Mr. **Kirtland**. My name is Grayson Kirtland. I retired June 1, 1978, from A.H. Robins Co. after a little more than 30 years of service. During most of my active employment, I was responsible for the development of the employee benefit program and administration.

Senator **Metzenbaum**. Do you want to pull the mike a little closer, please?

Mr. **Kirtland**. I am 70 years old and my wife is 59 years old. I am here before you today because I was selected by my fellow retirees as the cochairman of the ad hoc committee which represents the retirees' interests in the ongoing chapter 11 bankruptcy of A.H. Robins Co.

A.H. Robins is a business which was founded and is headquartered in Richmond, VA. A.H. Robins is principally in the business of manufacturing and marketing pharmaceutical products. The company has nearly 7,000 employees worldwide and does over $740 million in business per year.

Neither I nor my fellow retirees thought that we needed to be concerned about the future of our health benefits because we enjoyed a special relationship with our employer, and our employer promised us that those benefits would continue throughout our lifetime.

A.H. Robins was a healthy, successful pharmaceutical company until the late 1970's when claims engendered by the Dalkon Shield began to weaken the company's financial position.

Primarily as a result of the costs associated with this litigation, on August 21, 1985, Robins filed a petition of bankruptcy under chapter 11 of the Bankruptcy Code in the U.S. District Court for the Eastern District of Virginia.

The next day, all retirees and disabled former employees received a letter from E. Claiborne Robins, Jr., in which Mr. Robins, on the advice of expert bankruptcy counsel, assured us that our benefits were secure.

Ten short months later, on June 19, 1986, we received a second letter from Mr. Robins. The second letter informed us that according to new expert bankruptcy counsel, Robins could not continue our benefits under the bankruptcy laws.

At the same time, based on the new lawyer's interpretation of the bankruptcy code, Robins filed a motion to reject the contracts of insurance which covered Robins retirees and disabled former employees.

Soon after the June 19 letter, a representative group of Robins retirees and disabled former employees met and chose a nine-person ad hoc committee to represent the interests of the 329 retired or disabled former employees whose benefits were threatened. The ad hoc committee then hired a local law firm to represent the retirees in the bankruptcy proceedings.

I think it is appropriate to mention the special relationship which Robins employees enjoy with their firm because I believe it is a fairly unique situation. The Robins Co. was founded and continues to be managed on the principle that it is a family.

During my first years with the company, it was not uncommon to see Mr. E. Claiborne Robins, Sr., down on the floor of the plant mingling with the workers. In addition, on several occasions Mr. Robins shut down the plant and took the entire workforce on fully paid vacations to New York, Miami, and Havana. I know of no other major manufacturing corporation which engaged in a similar practice.

The result of this special relationship was that Robins employees enjoyed unusually high morale and unusually productive work lives. As an example of this family feeling, current employees of Robins, on learning of the plight of the retirees, raised approximately $10,000 to help the retirees pay their legal expenses in this connection.

At Robins, there has always been trust and commitment between management and the workforce. Because of this, there has never been a union, a collective bargaining agreement, or the need for either. This trust and commitment has been greatly harmed by the decision forced on the Robins Co. by their lawyers' interpretation of the bankruptcy laws to sever the medical, dental, and life insurance benefits of its retirees and disabled former employees.

Senator **Heflin**. Mr. Kirtland, we have the last call for our vote. Now, you have a written statement; all of it can be submitted for the record.

[Statement with attachment follows:]

# TESTIMONY OF GRAYSON KIRTLAND, CO-CHAIRMAN OF THE AD HOC COMMITTEE OF PRE-PETITION RETIRED AND DISABLED FORMER EMPLOYEES OF A. H. ROBINS COMPANY

My name is Grayson Kirtland. I retired June 1, 1978 from A. H. Robins Company, after a little more than thirty years service. During most of my active employment, I was responsible for the development of the Employee Benefit Program and its administration. I am seventy years old, and my wife is fifty-nine years old. I appear before you today, because I was selected by my fellow retirees as the co-chairman of the Ad Hoc Committee which represents the retirees' interests in the ongoing Chapter 11 bankruptcy of the A. H. Robins Company.

For your information, A. H. Robins is a business which was founded and is currently headquartered in Richmond, Virginia. A. H. Robins is principally in the business of manufacturing pharmaceutical products. The company has nearly 7,000 employees worldwide and does over $740,000,000 in business per year. Neither I nor my fellow retirees thought that we needed to be concerned about the future of our health benefits, because we enjoyed a special relationship with our employer, and our employer promised us that those benefits would continue throughout our lifetimes.

A. H. Robins was a healthy, successful pharmaceutical company until the late 1970's when claims engendered by the Dalkon Shield began to weaken the company's financial position. Primarily as a result of the costs associated with this litigation, on August 21, 1985, Robins filed a petition of bankruptcy under Chapter 11 of the Bankruptcy Code in the United States District Court for the Eastern

District of Virginia. The next day all retirees and disabled former employees received a letter from E. Claiborne Robins, Jr. in which Mr. Robins, on the advice of expert bankruptcy counsel, assured us that our benefits were secure. Ten short months later - on June 19, 1986 - we received a second letter from Mr. Robins (see Attachment "A"). The second letter informed us that, according to new expert bankruptcy counsel, Robins could not continue our benefits under the bankruptcy laws. At the same time, based on the new lawyers' interpretation of the Bankruptcy Code, Robins filed a motion to reject the contracts of insurance which covered Robins retirees and disabled former employees.

Soon after the June 19, 1986 letter, a representative group of Robins retirees and disabled former employees met and chose an eight person Ad Hoc Committee to represent the interests of the 329 retired or disabled former employees whose benefits were threatened. The Ad Hoc Committee then hired a local law firm to represent the retirees in the bankruptcy proceedings.

I think it appropriate to mention the "special relationship" which Robins' employees enjoy with their firm, because I believe it is a fairly unique situation. The Robins company was founded and continues to be managed on the principle that it is a "family." During my first years with the company, it was not uncommon to see Mr. E. Claiborne Robins, Sr. down on the floor of the plant mingling with the workers. In addition, on several occasions, Mr. Robins shut down the plant and took the entire work force on fully paid vacations to New York, Miami and Havana. I know of no other major manufacturing corporation which engaged in a similar practice. The result of this "special relationship" was that Robins' employees enjoyed unusually high morale and unusually productive work lives. As an example of this "family" feeling, current employees of Robins, on learning of the plight of the retirees, raised approximately 10,000 to help the retirees pay legal expenses. At Robins, there has always been trust and commitment between management and the work force. Because of this, there has never been a union, a collective bargaining agreement, or the need for either, at Robins. This trust and commitment has been greatly harmed by the decision, forced on the Robins Company by their lawyers' interpretation of the bankruptcy laws, to sever the medical, dental and life insurance benefits of its retirees and disabled former employees.

At the time of the filing of the Bankruptcy Petition, all of the members of the retiree group received medical and life insurance; a few also had dental insurance. The medical and dental coverage, which included dependents, was provided through Connecticut General Insurance Company, and the life coverage was through the Life Insurance Company of Virginia. According to statistics prepared by the Robins Company for the years 1984-1986 (see Attachment "B"), the company expended $300,000 to $400,000 per year in medical and dental coverage attributable to the pre-petition retirees and disabled former employees. This amounted to only 5.6%-6.1% of the total expenditures by the company for medical or dental benefits. The medical and dental coverages are "basic" coverages with a $100.00 annual deductible. In addition, the company expended between $50,000 and $160,000 per year in life insurance benefits to retirees and disabled former employees. This amounted to only 4.5%-25.6% of the total expenditure by the company for life benefits. Initially, a retiree's life insurance coverage is one and one-half times his wage at the time of his retirement. It decreases to 25% of that amount after five years of retirement.

I have been one of the lucky retirees. Neither my wife nor I has been sick prior to or since my retirement. After the decision of the Robins Company to cut off the benefits to retirees and disabled former employees, I looked into individual replacement health coverage for my wife and myself. Because my wife is only fifty-nine years old and thus receives no Medicare, I discovered that it would cost $1,041.67 in premiums per year with a $250.00 annual deductible in order for her to receive coverage similar to what Robins had provided. I received this quotation on insurance coverage from the American Republic Insurance Company, and found it to be a competitive insurance rate for someone in my wife's health and age classifications. I also looked for health coverage for myself. Because I am seventy years old, I only needed health coverage which would supplement Medicare. The Blue Cross/Blue Shield plan which I investigated charges $511.20 in premiums per year. Thus, our total out-of-pocket expense for replacement insurance coverage is $1,552.87 per year. This is a sum which we had not budgeted for and did not expect to have to pay, because the Robins Company had promised that our benefits would continue during our lifetimes.

All the retirees have had difficulty in acquiring replacement medical coverage. Many of my colleagues found themselves with serious or terminal illnesses at the time the company threatened to cut off our benefits. For many, there was no way to obtain coverage for these pre-existing conditions. I know of one Robins retiree who is 90 years old. His age alone prevents him from obtaining replacement coverage. In addition, nearly all the retirees are prevented from obtaining life insurance by the prohibitive costs.

As I mentioned previously, I am one of the lucky ones. In preparing for the hearings in the Bankruptcy Court concerning our benefits, the Ad Hoc Committee and our lawyers solicited information from fellow retirees and disabled former employees. The reports we received were most distressing. Twelve retirees have died since August 21, 1985. If our benefits were cut off, the spouses or dependents of those retirees would be left without those life benefits. In many cases, the cost of a simple funeral would become too much to bear.

In addition, we received reports from a number of retirees who faced catastrophic illnesses. Below are excerpts from letters sent to the Committee and its lawyers by Robins retirees (the names have been omitted):

1. In a letter from the son-in-law of a retiree:

> Mr.____ worked for the A. H. Robins Company, Inc.(Robins) for twenty-three years as a sales representative. He was asked to retire from the company in August, 1980. At that time and prior thereto, he was promised full benefits, including life insurance to age sixty-five, medical insurance to age sixty-five, and pension rights. From 1980 to 1985, Mr. _____ did not obtain any other insurance based on Robins' assurances of continued coverage. After Robins filed for bankruptcy in 1985, Mr. _____ specifically did not obtain other insurance based on the assurances in Robins' August 22, 1985 letter.
>
> On January 2, 1986, Mr._____ experienced the first of several convulsions. After several months, he was diagnosed as having a malignant brain tumor. Mr._____has undergone several expensive diagnostic tests, surgery and will undergo extensive treatment, including radiation and chemotherapy in the future. The

expense for Mr._____'s treatment thus far and in the future will be exorbitant.

2. In a letter from a retiree who worked thirty-two years:

    I will be 74 years old in a few months and due to High Blood Pressure, I cannot get Life Insurance. This has really worried me and has put a hardship on me because this was all the Life Insurance I had to bury me.

    All I have is Medicare and that is not taking care of my medical expenses. In April and May, 1986 I was really sick with arthritis, and had to have medication, and therapy treatments. My doctor has said that I may have to have an operation later because of the deterioration of the bone in my neck pressing on the nerves. This is a very painful sickness and experience.

    I lost my left eye (have glass eye) due to acute glaucoma and pressure build-up a few years ago. I have to go to Charlottesville regular (sic) to have right eye checked because of cataract and just got new glasses another expense. The doctor in Charlottesville have done (sic) laser on the right eye, watching the pressure and doing everything they can trying to save this eye. Every year I have to go now having the glass eye checked.

3. A letter from the widow of a retiree of Chapstick (a company bought out by Robins):

    Wilford, my husband, was so ill and almost at death's door that I couldn't tell him what happened to his medical and life insurance. He was going through enough without him having to know that. He had always told me that if he died I wouldn't have to worry - his insurance would take care of me.

    I am now faced with a $3,715.20 funeral expense and $1,650.18 for doctor's expense plus some other things that occurred.

4. In a letter from the same retiree's daughter:

    I have been so upset over what this thing with A. H. Robins has done to my Mother during her time of despair. I could not believe that something this awful could happen in this country. While my Father was dying with cancer and she was in anguish over taking care of him and seeing to his needs she received a letter saying he was no longer covered with hospitalization or life insurance. She received the letter in the midst of getting him out of

> the hospital (they had sent him home to die), while the ambulance people were bringing him into the house she was reading the letter about Robins. Needless to say she went through absolute Hell with worry and when they had to take him back to the hospital within the week she almost had a nervous breakdown. The neighbors had to come to her rescue since she was in Virginia and my brother and I live in Florida and were not aware of the troubles she was experiencing. She was crying hysterically that they could not take him back to the hospital even though he was in a coma and the ambulance was trying to take him there, because "I have no insurance, I can't pay for it, what am I going to do". How sad and unjust! I feel very fortunate that my Mom did not die from a stroke during this time. She has elevated blood pressure and it could very easily have happened in reality. They kept my Dad in the hospital until he stabilized and sent him back home, this time to die. During all this time my Mother was in a daze over the overwhelming horror of it all. At first I thought it was so sad that the cancer had invaded my Dad's brain and he was not aware of half of what was going on but later after all this happened I know that God was looking after him.

5. In a letter from a Robins retiree:

> On June 7, 1986, my wife entered the hospital for colon surgery with the comforting knowledge that we were fully covered by Medicare and my Robins insurance. She was discharged on June 20 to find that, on early information, our policy was cancelled as of the previous day. This caused two months of severe anxiety until we were able to secure new insurance.
>
> I have paid out, so far, $1,188.78 for bills that Medicare did not cover and am waiting to see how much Connecticut General paid.
>
> I expect further follow-up visits will cost at least $500.00 and not be covered by our new insurance.

6. From a Robins retiree who had worked for thirty-eight years and two months:

> On May 20, 1986, my wife fell and fractured her left hip. This required surgery and 8 days hospitalization - approximately $8,000 in medical bills. However, due to the accident occurring before June 21, 1986 the

majority was covered by Connecticut General Life Insurance Company. After receiving Mr. E. C. Robins', Jr. letter informing us that the Company would no longer cover our medical and dental insurance needs, I applied for medical coverage for my wife since she is not eligible for Medicare. I was successful in securing a policy; however, we had to accept a waiver against any future hip injuries. The cost is $82.30 per month. Since I am COVERED BY Medicare, I had to buy supplement insurance - cost of $38.25 per month.

As you can see from the above information Health Insurance is now costing us $1,500 a year and we don't have as much coverage as under the Company policy - but it's the best we can get.

If the total program is not reinstated, I will also lose Life Insurance which is part of my estate plans. At my age I could not afford to buy more life insurance - even if I could get it.

7. From a Robins retiree:

I was admitted to Retreat Hospital on Nov. 4, 1985 complaining of chest pains and another more indefinite pain. It was diagnosed that I have angina pectoris and gallstones. On Nov. 7, I was transferred to Chippenham where I had an angioplasty. There was no further treatment at that time for the gallstones. I was discharged from Chippenham on Nov. 11, 1985. The charge was approximately $8,000 or $9,000. Medicare paid part and also Conn. Gen. Although as you know we have been told that we may have to repay the amount paid by Conn. Gen. I paid approx. $1,000.

8. From a Robins retiree:

My wife have (sic) a cancer found 3/3/86 and was admited (sic) to Richmond Metropolitan Hospital on 3/4/86 thinking what Medicare didn't take care of Conn. General Life (sic) Insurance Co. would.

Up to now the insurance Co. have pay (sic) most of the Part but the thing that worry (sic) me is we may have to Pay it back.

She also have (sic) Alzheimers disease and I am afraid I will someday have to put her in a nursing home. If I had known I was

> not Protected by Robins after they Promised
> to do so I would made (sic) other Points
> toward Protection.

These letters only provide examples of the problems that Robins retirees and disabled former employees have faced. The majority of Robins retirees are former plant workers who hold small pensions. For those individuals, a small, fixed income and pre-existing health conditions combine to make them entirely dependent on the benefits which Robins provided. They do not understand how their compensation for lifetimes of service can be taken away under the bankruptcy code, especially when the company continues to show a profit and wants to continue the benefits.

Fortunately, Bankruptcy Judge Blackwell Shelley and District Court Judge Robert Merhige chose to continue our benefits until May 15, 1987 based on the temporary appropriations bill adopted by Congress. After May 15, we do not know what will happen to our benefits.

I have seen the proposed amendment to the Bankruptcy Code. I am not and do not profess to be, an expert bankruptcy lawyer, but I do believe that provisions like those in the amendment which permit the court and the bankruptcy debtor to continue benefits to retirees if the continued financial health of the debtor company is not endangered are exactly the type of provisions which will enable non-union retirees to feel secure about their benefits without compromising the rights of other creditors too severely.

In conclusion, I do not believe it is right or fair that after spending most of their lifetimes working for a company, retired people should find themselves suddenly without any security. The bankruptcy law as currently written totally ignores the needs and rights of nonunion retirees. I believe that retirees have the right to be treated in a fair and compassionate manner. That is all anyone could ask.

Thank you for your time and attention.

E. Claiborne Robins, Jr.
President and Chief Executive Officer

A. H. Robins Company
1407 Cummings Drive
P. O. Box 26609
Richmond, Virginia 23261-6609
Telephone (804) 257-2287

A·H·ROBINS

Mr. Grayson M. Kirtland
Route 2, Box 179 B
Heathville, VA 22473

June 21, 1986

Dear Grayson:

As you will recall, following the filing of the Company's petition for Chapter 11 reorganization, we sent you a letter dated August 22, 1985 in which we explained the reasons for the filing. Additionally, we informed you that benefit programs for retired employees of the Company would not be affected by filing. That assurance was based upon legal advice given to us at that time.

On March 28, 1986, the U. S. District Court for the Eastern District of Virginia directed the Company to recover all payments made after August 21, 1985 on account of obligations existing on or before that date. U. S. District Court Judge Robert R. Merhige, Jr., indicated that this action is mandated by law and to date has declined to afford any relief for any class of recipients.

We have now been advised by our current bankruptcy counsel that payments made from general operating funds of the Company to provide medical and other insurance benefits for employees whose active service terminated on or before August 21, 1985 are within the scope of the Court's March 28, 1986 directive. Similarly, any other payments made to or on behalf of retired employees or eligible dependents are also regarded as post-petition payments on pre-petition obligations. In compliance with the Court's directive, the Company must discontinue any further payments for these purposes and is obligated to recover amounts paid after the filing.

As a consequence, the Company will no longer be able to provide medical, dental or life insurance benefits for former employees whose active service terminated on or before August 21, 1985, and their eligible dependents. Furthermore, during the course of the reorganization case, the Company will not be able to make payments such as birthday checks or other supplemental retirement gratuities and will be required to recover amounts paid since the filing date.

85-01307-R
EXHIBIT 3
ATTACHMENT A

A. H. Robins Company

Medical and Dental Plan Expenses

(Based on Conventional Premium Cost for Retirees)

| | Medical | Dental | Total | Percentage of Liability |
|---|---|---|---|---|
| 1986 Projected | | | | |
| Active | $5,407,811 | $617,428 | $6,025,239 | 94.0% |
| *Retired | 360,084 | 24,578 | 384,662 | 6.0% |
| | $5,767,895 | $642,006 | $6,409,901 | 100.0% |
| 1985 (Actual) | | | | |
| Active | $4,658,568 | $642,015 | $5,300,583 | 94.4% |
| *Retired | 292,140 | 24,156 | 316,296 | 5.6% |
| | $4,950,708 | $666,171 | $5,616,879 | 100.0% |
| 1984 (Actual) | | | | |
| Active | $3,932,997 | $601,718 | $4,534,715 | 93.9% |
| *Retired | 271,791 | 21,953 | 293,744 | 6.1% |
| | $4,204,788 | $623,671 | $4,828,459 | 100.0% |

Note: 1. Figures Do Not Include Claims Experience of Subsidiaries

*2. Retired class includes only the affected group

3. Actual claims experience for retired employees not separately tracked until 1986. Above figures on retirees are based upon conventional premium cost.

85-01307-R
EXHIBIT 1
ATTACHMENT B

## Life Insurance Claims Expenditures

| | Actual Number of Death Claims | Actual Death Claim Payments | Projected Death Claim Payments for Remainder of Year | Estimated Administrative Expenses | Estimated Retro-call Expenses | Projected Total Cost | Percentage of Liability |
|---|---|---|---|---|---|---|---|
| **1986 (Projected)** | | | | | | | |
| Active | 4 | 556,500 | (1) 397,500 | 42,536 | 135,822 | 1,132,358 | 87.6% |
| Retired | *7 | *83,069 | (1) 59,335 | **4,156 | **13,269 | **159,829 | **12.4% |
| | 11 | 639,569 | 456,835 | 46,692 | 149,091 | 1,292,187 | 100.0% |
| **1985 (Actual)** | | | | | | | |
| Active | 8 | 858,374 | N/A | 42,536 | 198,408 | 1,099,318 | 95.5% |
| Retired | 6 | 28,925 | N/A | **4,156 | **18,195 | **51,276 | **4.5% |
| | 14 | 887,299 | | 46,692 | 216,603 | 1,150,594 | 100.0% |
| **1984 (Actual)** | | | | | | | |
| Active | 4 | 237,206 | N/A | 33,996 | -0- | 271,202 | 74.4% |
| Retired | 6 | 92,325 | N/A | **1,124 | -0- | **93,449 | 25.6% |
| | 10 | 329,531 | | 35,120 | -0- | 364,651 | 100.0% |

Note: * Five of the Death Claim Payments Totaling $34,094 are in a Pending Status

** Estimated Expenses and Total Cost for Pre-Petition Retirees

Assumptions:
1. Assumes death experience in last 5 months of 1986 will be mirrored from experience in first 7 months of 1986.
2. This chart is reflective of experience for A. H. Robins Company, Inc. and its subsidiaries whose employees participate in the Group Life Insurance Plan.

## SCENARIO

(All Active and Retired Employees Die on the Same Day)

June, 1986 Data

| | Number of Lives | Total Life Insurance In Force | Percentage of Liability |
|---|---|---|---|
| Active | 3,235 | $271,407,500 | 96.3% |
| Retired Prior to 8/21/85 | 280 | 7,268,000 | 2.6% |
| Disabled Prior to 8/21/85 | 44 | | |
| Retired After 8/21/85 | 86 | 3,074,982 | 1.1% |
| Disabled After 8/21/85 | 0 | | |
| | 3,645 | $281,750,482 | 100.0% |

Note: Information verified by Life Insurance Company of Virginia on August 4, 1986.

Senator HEFLIN. We are going to have to recess this hearing now for a little while until we can go over and vote, then come back. [Recess.]

Mr. Kirtland, did you want to conclude in about a minute? You may place all of that in the record for everybody to read.

Senator Metzenbaum is having to attend a rally so he is not here right now.

VOICE. We want to get to the rally also.

Mr. KIRTLAND. I will skip quite a bit if you want me to. I will pick up a few things though.

One is some of the retirees have had difficulty in acquiring replacement medical coverage because of hospitalization cancellation coverage. Many of my colleagues found themselves with serious or terminal illnesses at the time the company threatened to cut off our coverage. For many, there was no way to obtain coverage for these preexistent conditions.

I know of one Robins retiree who is 90 years old. His age alone prevents him from obtaining replacement coverage. In addition, nearly all the retirees are prevented from obtaining life insurance because of prohibitive cost.

I have several letters I will have in the report here from retirees who are very distressed about the financial condition they found themselves in and their health conditions.

There is one thing I would like to point out. It is hard for us to understand, sir, why prepetition retirees are canceled out and post-petition retirees continue. In other words, someone retiring a day before a company files under chapter 11 loses their benefits, whereas someone retiring a day after, they are able to keep theirs. That does not make a whole lot of sense to us.

I have seen the proposed amendment to the Bankruptcy Code. And, of course, I have not been trained in the legal profession. However, I do believe that provisions like those in the amendment, which permit the court and the bankruptcy debtor to continue benefits to retirees, if the continued financial health of the debtor company is not endangered are exactly the type of provisions which will enable nonunion retirees to feel secure about their benefits without compromising the rights of other creditors too severely.

In conclusion, I do not believe it is right or fair that after spending most of their lifetimes working for a company, retired people should find themselves suddenly without any security. The bankruptcy law, as currently written, totally ignores the needs and rights of nonunion retirees.

I believe that retirees have the right to be treated in a fair and compassionate manner. That is all anyone could ask.

Thank you for your time and attention.

Senator HEFLIN. All right. Our next witness is Ms. Lillian Lemmens.

Ms. Lemmens.

## STATEMENT OF LILLIAN LEMMENS

Ms. LEMMENS. Honorable Senator, I am proud to be here today to try and express what it means to me to have medical insurance, pension and life insurance.

I had worked for Republic Steel Corp., now LTV, for 33 years as a non-bargained-for employee before retirement. Last July, LTV declared bankruptcy and, therefore, we would no longer get our benefits. We are entitled to these benefits, as they were part of our salary.

My bosses at Republic Steel always told me that not to worry, we would always have a pension, medical insurance, and life insurance as the money was vested for us.

I am only one of thousands of salaried non-bargained-for employees that is affected by no benefits after May 15. A very good example of why we need the benefits: in May of 1985, my husband became suddenly ill with cancer. At that time, all the bills were paid by the medical insurance, and then LTV went into bankruptcy. When the checks could not be cashed, but later, with the help of Senator Metzenbaum and others, LTV gave us an extension until this May 1987.

Here is an approximate summary of the expenses that we would have had to pay if we did not have medical insurance. Hospital cost, $67,564; physicians, $40,047; x rays, $4,239; therapeutic, $2,862; pathology, $387; prescriptions, $840; total, $115,939.

One physician's fees alone came to over $31,619. These expenses covered 1½ years of sickness. When my husband passed away November 7, if I had to pay these expenses, what would have happened? No doubt I would have had to sell my home and go into our savings. As for pension, I am still receiving mine through the Pension Benefit Guarantee Corp.

The thousands of non-bargained-for salaried employees and I would be most grateful, Honorable Senator, if you could arrange for the retirees to continue to receive our medical insurance, pensions, and life insurance, what is really due us. Please find it in your heart to help us.

Thank you.

Senator **HEFLIN**. Thank you very much.

The next witness is Ms. Kathryn O. Hunt.

## STATEMENT OF KATHRYN O. HUNT

Ms. **HUNT**. Thank you, Senator.

I am here in behalf of my husband that worked for LTV for 29 years. And I have a 75-year old baby that I take care of.

The day that I received the letter that stated he no longer has hospitalization or insurance, I was waiting for a doctor to come to my home because my husband was running a fever of 105, and he has respiratory trouble. The doctor came, and he says, well, Mrs. Hunt, the only thing we can do is to rush him to the hospital. I says no way. He said what do you mean? I had no insurance. I showed him the letter, and he just shook his head, and he said but you are taking a chance. He says, you know, I will not be responsible.

I took care of him. I still take care of him. And I am worried. What is going to become—where am I going to get the money to get him in a medical insurance or life insurance at this date? After 29 years of working there, I think the company owes not only my husband, Eddie, but there are a lot of Eddies, there are a lot of wives, there are a lot of husbands that are taking care of our wives that have just got insurance. You cannot purchase or afford even insurance for myself, which I am a few years younger than him.

So I beg of you, Senator, I am in Mr. Stokes' district, the 21st District in Cleveland. I have talked with him so I present my worries to you, and I hope that you take care of all of our little worries that are quite big.

Senator **HEFLIN**. Thank you. We appreciate your testimony.

Our next witness is Mr. Nathan B. Feinstein of the American Bar Association's Corp., Banking and Business Law Section of Philadelphia, PA.

## STATEMENT OF NATHAN B. FEINSTEIN, AMERICAN BAR ASSOCIATION, CORPORATION BANKING AND BUSINESS LAW SECTION, PHILADELPHIA, PA

Mr. **FEINSTEIN**. Thank you, Senator Heflin.

My name is Nathan B. Feinstein. I am the partner in charge of the bankruptcy and workout practice of the Philadelphia law firm of Dilworth, Paxson, Kalish and Kauffman. I am here today to present a position of the American Bar Association's Corp., Banking and Business Law Section. I chair the chapter 11 subcommittee of the Business Bankruptcy Committee of that section.

No sensitive person can view with equanimity the limitation of a retiree's rights. Those who have labored a lifetime in the expectation of a retirement secured by payments under pension plans and health benefit programs are entitled to the assurance that their rational economic expectations will not be thwarted. One must associate himself with the remarks of Senator Heinz and even of Mr. Williams and others who suggest that a rational approach to the problem is required.

One can even be outraged at the conduct of LTV or A. H. Robins in unilaterally terminating health coverage to retirees. It is probably wrong, probably outrageous and may even have been dumb. But that is not the issue. The question before the Senate is whether the Bankruptcy Code, and particularly the corporate reorganization sections of chapter 11 is where the social policy of protecting retirees should be implemented.

I respectfully suggest that, if enacted, the provisions of section 548 will prove to be counterproductive.

The use of Bankruptcy Code amendments to address the problem of funding retirement benefits is haphazard at best. It could be disastrous to the chapter 11 process.

A retiree benefit program linked to chapter 11 only discourages the use of chapter 11. One can liquidate in a variety of other ways. One can liquidate under State law; one can liquidate in chapter 7; one can liquidate by allowing an indenture trustee to take over the assets of a company. The creation of new and uncertain priorities . . . which may threaten secured lenders . . . will clearly raise the cost and decrease the availability of financing, particularly the hard-pressed companies. In the long run, it will impel lenders to simply require in their lending instruments that borrowers not enter into plans that provide benefits which are not fully funded. The effect would be to sharply limit the availability of those benefits.

The addition of a large and potentially overwhelming class to the cost of administration priority will severely limit the availability and significantly increase the cost of goods and services during the chapter 11 process: that time when it is critical for a debtor to be able to either arrange for borrowings or to arrange for people to sell to it so it can continue in business.

Perhaps most significant, S. 548 distorts a workable and equitable bankruptcy distribution pattern fashioned over three-quarters of a century of experience with the Federal bankruptcy law. A major reason that the bankruptcy reorganization process works in the United States and does not work in virtually every European country is that the U.S. pattern limits priorities rigidly. In France, where virtually the entire welfare system is larded into what would be the equivalent of the chapter 11 process or reorganization process as a priority, the result is that one simply does not use reorganization.

The same thing is true in Great Britain where there has been the growth of the floating charge to take the reorganization process out of the judicial process: that which would be the equivalent of chapter 11.

The only time that it has worked in those countries is when the Federal Government, in France or in England, has stepped in and provided the funds to keep the retiree benefits or other labor aspects of a terribly pressed industry functioning. Indeed, in our

American experience, the one time this was really done was in the Northeast Railroad reorganization. And Congress stepped in—the reason it worked was Congress stepped in and realistically funded the retiree benefits.

The simple fact is that the comments accompanying the introduction of S. 548, referring to LTV and Robins, were just off base. Those comments suggested that in chapter 11 reorganizations, the competing claims are those of the employer company, shareholders or what have you, on the one hand, versus the claims of retirees. That is simply not the case. The invariable bankruptcy policy—the policy deeply rooted in constitutional principles—is that the owners of a chapter 11 debtor may not receive anything or retain anything of value under a plan of reorganization unless the various classes of creditors, and that would include even retirees today, have been paid in full or have consented.

The real competition in a case like A. H. Robins would be between the claims of retirees who, if given a cost of administration priority would get paid in full, and the unsecured creditor body, which is made up of women unfortunate enough to have used interuterine devices. Is the Congress prepared to say that it is going to give 100 percent priority to retired employees when that money comes out of the funds which might otherwise be available to pay the A. H. Robins' victim claims?

The same thing could be said of Manville. In the *Manville* case, if you had the same set of facts going, the question would be whether those people who have breathed asbestos over the years are going to be relegated to a lower category. Has Congress made a decision that it is correct to relegate them to a lower category then the retired employees (who probably are in the same category in part)?

The same thing could be said of environmental claims, the other major kind of problem that is putting many companies into chapter 11. The major question of how our economy today is going to deal with a transition of what was formerly a labor intensive industry to a technologically efficient industry is a major economic and social problem. It is precisely in those industries where the impact of S. 548 would be greatest. The only way those companies can reorganize is if during the chapter 11 they are permitted to use their scarce funds to function on at least a break-even basis. If one sees that they can function on a break-even basis without paying prepetition or other liabilities, then you know you have a kernel around which you can build a reorganization. If you take the scarce funds available and put them to the benefit of just one category, what you are doing is making it impossible for those companies to reorganize in chapter 11. They will find other imaginative ways to do it.

S. 548 itself does a number of really questionable things. It elevates medical and disability retiree claims, which arise out of prepetition contracts, to a cost of administration or first priority status, but only those that come due during the postpetition chapter 11 period. It removes the 1-year damages limitation of section 502(b)(7) from the pension claims of retirees covered by collective bargaining agreements, but not for retiree claims of retirees not covered by collective bargaining agreements, thus sharply distinguishing between union and nonunion retirees.

It removes the 1-year damage limitation of 502 from medical and disability claims which arise under plans or programs, but not from those which arise under individual employment contracts. It makes unions presumptively the authorized representatives of retirees, disregarding the inherent conflict between those bargaining for the day-to-day survival of current jobs and the more indirect interest of retirees.

The way the bill works is if the union is prepared to function, it functions. It takes over that role. It creates a hearing process——

Senator **HEFLIN**. Summarize your statement in about a minute.

Mr. **FEINSTEIN**. I am sorry, Senator.

Senator **HEFLIN**. Go ahead.

Mr. **FEINSTEIN**. Senator, I will finish up in about 1 more minute.

What S. 548 will do, if enacted, is that it would require any debtor contemplating chapter 11 to use another process for reorganization, or to move immediately under the proposed sections 1113 and 1114 to reduce retiree benefits. One would have to do it immediately because the failure to do that would build up a class of administrative claims which would then make it impossible in virtually every instance to reorganize that company. It would put one entrenched class ahead of all other classes. If that happens, what we are going to do is compel companies, before they have really made an assessment of how or whether they can reorganize, or whether they can pay retiree claims during the process, to immediately move to reject under 1113 and 1114.

There is also a serious question about the constitutionality of the proposed legislation.

I would most strongly urge that the Congress defer acting on the quick fix presented by legislation like S. 548. It fails the most simple tests. It is ill conceived. It will not work to further the goals it purports to reach. It is probably bad social policy to use S. 548 as an excuse for not doing what really has to be done for all workers. And it threatens the utility of a chapter 11 process which currently does work.

On behalf of the corporation, banking and business law section of the ABA, we thank you for having had us here. If there is some way that we can provide, from the body of expertise that we have, some assistance in reformulating possible solutions to this bill, we certainly would be happy to try to provide that assistance.

Senator **HEFLIN**. Rather than asking the questions, we will submit them in writing, and it may well be that at the next hearing we may call on you again.

[The following material was submitted for the record:]

# TESTIMONY OF NATHAN B. FEINSTEIN
# PRESENTING THE POSITION OF THE
# AMERICAN BAR ASSOCIATION'S
# CORPORATION, BANKING AND BUSINESS LAW SECTION
# ON SENATE BILL 548

My name is Nathan B. Feinstein. I am the partner in charge of the bankruptcy reorganization and work-out section of the Philadelphia law firm of Dilworth, Paxson, Kalish & Kauffman. I serve as chairman of the Chapter 11 Subcommittee of the Business Bankruptcy Committee, one of the largest committees in the Corporation, Banking and Business Law Section of the American Bar Association.

There are more than 50,000 members of the Corporation, Banking and Business Law Section. They are engaged in every aspect of representing clients in business matters. The Business Bankruptcy Committee is comprised of close to 500 lawyers covering the entire field of bankruptcy law, including the representation of debtors, creditors, individual claimants, unions, and institutional lenders. The position adopted by the Business Bankruptcy Committee, and thereafter approved by the Corporation, Banking and Business Law Section, was virtually unanimous -- a rare occasion indeed.[1] Although the initial focus of that position was the Metzenbaum Amendment which emerged as Section 608(a) of Public Law 99-591, the substantive position is paralleled by the concerns expressed here regarding S.548.

No sensitive person can view with equanimity the limitation of a retiree's rights. Those who have labored a lifetime in the expectation of a retirement secured by payments under pension plans and health benefit programs are entitled to the assurance that their rational economic expectations will not be thwarted. Defects, real or imagined, appear in the Pension Benefit Guaranty Corporation and related pension guaranty legislation, and particularly in their funding. Proposals to assure adequate funding, or even to provide governmental funding, abound, and many are worthy of serious consideration. Legislation offering tax incentives for pre-funding retiree death, disability and health benefits should be given high priority. Consideration should be given to removing the disincentives created by tax changes in 1984. A humane government and a compassionate social policy must provide for those who have been "retired" by reason of age, infirmity, or economic dislocation. One cannot help but share the instinct that impelled the introduction by Senator Metzenbaum, my own Senators Heinz and Spector, and the other co-sponsors of S.548; a reaction to what they considered to be the unfortunate or even outrageous conduct of LTV or the A.H. Robins in unilaterally terminating health coverage to retirees.

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[1] The matter was not submitted for approval by the American Bar Association.

But that is not the issue. The question before the Senate is whether the Bankruptcy Code -- and particularly the corporate reorganization provisions of Chapter 11 -- is the place where the social policy of protecting retirees should be implemented. We respectfully suggest that it is not, and that, if enacted, the provisions of S.548 will prove to be counter-productive.

The use of Bankruptcy Code amendments to address the problem of funding retirement benefits is haphazard at best and could be disastrous to the Chapter 11 process. A retiree benefit priority linked only to Chapter 11 discourages the use of Chapter 11. The creation of new and uncertain priorities which may threaten secured lenders will raise the cost and decrease the availability of financing. In the long run, it will impel lenders to require that borrowers not enter into plans that provide benefits which are not fully funded; the effect being to limit sharply the availability of those benefits. The addition of a large and potentially overwhelming class to "cost of administration" priority status will severely limit the availability, and significantly increase the cost, of goods and services to Chapter 11 debtors. Perhaps most significant, S.548 distorts the workable and equitable bankruptcy distribution pattern under current law.

Fair and equitable treatment of creditors' claims is a primary goal of the bankruptcy process. The goal is implemented through a delicate balancing of the claims of those who advanced goods or moneys to the debtor or who entered into contractual undertakings with the debtor prior to the filing of the bankruptcy petition; those who extended credit secured by a portion of the debtor's assets in ways permitted by law; and those who will be called upon after the bankruptcy filing to provide goods and services to the post-petition debtor, including those who may be called upon to advance post-petition financing for the continued operation of the debtor. In a reorganization proceeding, all of those interests are in turn matched against the requirements of those who may be called upon to fund a plan of reorganization or to provide services or goods to a reorganized enterprise. That balance has emerged after almost a century of experience with bankruptcy laws in the Bankruptcy Code sections dealing with priorities (11 U.S.C. §507);

in limitations on certain categories of claims (e.g. 11 U.S.C. §502(b)(6) and (7)); in careful definition of claims (11 U.S.C. §101(4)) and their allowance (11 U.S.C. §502), including taxes (11 U.S.C. §505); in the determination and extent of secured status (11 U.S.C. §506); and in the careful regulation of post-petition expenses (11 U.S.C. §503) and of those who render post-petition services to the debtor (e.g. 11 U.S.C. §504 and 11 U.S.C. §§326-331). Why retired employees should now be preferred over other unsecured creditors is not explained.

A major reason that the bankruptcy laws, and the reorganization processes in particular, have worked well in the United States is that priority payments have been relatively limited. In many foreign countries those priorities have been extended to include substantial portions of the entire welfare system, and the reorganization process simply does not work. When the required priority payments to post-petition providers of goods and services, pre-petition employees, taxing authorities, customers or other claimants become too extensive, it becomes impossible to reorganize the enterprises (unless with the infusion of significant governmental assistance), or even to assure a reasonable distribution to unsecured creditors in liquidation. In England, therefore, there has been the growth of the "floating charge" under which banks or similar institutions take possession of all of an insolvent debtor's assets and proceed to liquidate or reorganize outside of the bankruptcy process, generally without significant judicial supervision. In France, and indeed in most other countries, reorganization is rare unless by the substantial infusion of governmental moneys. The one major American experience with reorganization coupled with extensive retirement benefits, that of the Northern railroads, required substantial governmental subsidization.

The crucial question in almost every Chapter 11 is: Are there portions of the debtor's operations which can be rehabilitated if they are relieved from the burden of past errors? In Chapter 11, the debtor is relieved of non-production payments for a limited period of time to see which of its operations are truly viable. The debtor is not relieved of his non-production obligations, but payments may be suspended temporarily. If there is a kernel that will prove profitable, that kernel may form the basis for reorganization; hopefully a reorganization that will provide the pre-petition creditors with more than they would receive in liquidation.

The Chapter 11 provisions of the United States Bankruptcy Code work well largely because the "delicate balance" of claims and priorities is further subjected to a negotiating process which impels each claimant or category of claimant to assess carefully the relative worth of their claims against the value of having the debtor emerge as a viable enterprise, thus preserving the going concern value of its assets, the jobs of its employees, and the contribution of its products and services to its community. Trade creditors, for example, may logically determine to take a lesser amount for their pre-petition claims in the expectation that a viable customer will emerge from the Chapter 11 proceedings. Laborers and other employees will often agree to a variety of adjustments in their pre-petition claims and their post-petition requirements in order to preserve the enterprise and the jobs associated with it. If a particular claimant or a category of claims proves unduly recalcitrant, Chapter 11 empowers the courts in certain instances to compel the acceptance of rational results.

Legislation such as S.548 distorts the process and thwarts the prospect for reorganization of Chapter 11 debtors. Section 507(a)(4) of the Bankruptcy Code as enacted in 1978 provides a limited priority for contributions to an employee benefit plan. The excess claim (that is, unpaid contributions in excess of the priority portion) is another category of claimant whose legitimate interests are tempered by the Chapter 11 negotiating process. The requirement that a Chapter 11 debtor continue to pay retired employee benefits in full notwithstanding the effect of those payments on the availability of cash for laborers providing current services to the post-petition debtor, or suppliers whose products are required for the continued operation of the post-petition debtor, or on banks or other funding sources who are asked to supply operating cash to the debtor, simply encourages retired employees to be recalcitrant, and the others to withhold their goods, services or financing. If funds are unavailable to pay for the continuing operations of the debtor, neither retired employees nor anyone else will benefit. If retired employees are given full payment of their pre-petition contract benefits during the Chapter 11 administration, no other category of claimant will agree to scale down or defer its pre-petition claims or permit assets to be expended to allow the post-petition operation to continue. The retired employees benefit provisions of S.548 simply creates one category of entrenched claimant whose demand on limited assets will tend to encourage rigidity in every other claimant group.

The immediate post-petition period is always crucial to a Chapter 11 debtor. Suppliers of goods and services will generally require cash payment, at least until they are satisfied that the debtor is viable and will be able to pay costs arising in the Chapter 11 administration. Employees, already shaken by the possibility of job loss, require current payment for their services and the prospect of continued employment for their loyalty. Customers require assurance that their suppliers will continue in business and will meet service and warranty obligations, or else they will shop elsewhere. (An oft forgotten truism is that "no customers, no business; no business, nothing to reorganize"). The addition of a heavy cost not associated with the current production of goods and services upon a debtor struggling to survive will often spell the difference between that debtor's ability to continue in operation pending reorganization, or its immediate liquidation.

The incorporation of the S.548 into the provisions of Chapter 11 will compel many debtors to seek (or many creditors to force a debtor to seek) the liquidation provision of Chapter 7 of the Bankruptcy Code -- to which the enactment does not apply -- as a means of preserving the debtor's assets. This will be especially true in a labor-intensive industry where the number of retired employees, hence the cost, would be greatest (and, of course, the number of current employees put out of their jobs by a liquidation most serious). In a close case, therefore, the enactment will almost always prove illusory.

The simple fact is that the comments accompanying the introduction of S.548 were off base. Those comments suggest that in Chapter 11 reorganizations the competing claims are those of the employer company and its shareholders versus the claims of the retirees. That is simply not the case. The invariable bankruptcy policy -- a policy rooted in constitutional law principles -- is that the owners of a Chapter 11 debtor may not receive or retain anything of value under a plan of reorganization unless the various classes of creditors -- and that would include retiree claims today -- have been paid in full or have consented. (There is a judicially-created exception where the owners or shareholders put new value into the reorganization debtor for a continuing interest.) That rule, known as the "fair and equitable" rule, is the keystone of Section 1129, the confirmation section of the Bankruptcy Code, as it was of the Bankruptcy Act which preceded it.

The real competition is among the various classes of creditors, and that includes the current employees of a Chapter 11 company and those who now assert a right to high priority for their retiree benefits. It should also be noted that S.548 would have no significant adverse impact on Wall Street bankers or other secured creditors. The right of the secured creditors (usually banks, insurance companies, and other institutional investors) are essentially unaffected by S.548. The real victims of S.548 would be the unsecured creditors and the prospect for reorganization: a prospect of the utmost significance to employees, to the communities in which the companies are located, and to our national economy.

Take, for example, the A.H. Robins case, repeatedly referred to in the introducing comments, or a hypothetical John Manville case (assuming that it had a substantial group of retirees). The major group of unsecured creditors in the Robins case are those unfortunate enough to have suffered toxic shock from the use of interuterine devices. In Manville, it is those persons, largely Manville employees or the employees of asbestos installers, who inhaled what we now know to be lethal fibers. To provide, as S.548 does, that it will be virtually impossible to terminate or limit retiree benefits, and that all such benefits will be raised to the first priority "cost of administration" category, is to say that Congress has determined that retired workers are to be paid in full (if the debtor's assets are sufficient), and that the injured tort claimants are to be paid not at all or only what is left.

Consider troubled companies that have polluted or which may continue to pollute. While there are current disputes respecting the extent to which the claims of environmental agencies are to be deemed costs of administration, is S.548 a Congressional declaration that the claims of retired employees are to be on a par with certain environmental claimants, and are to come ahead of a large category of environmental claims? A similar question may be asked in respect of unsecured creditors, usually small businessmen unable to exercise the economic clout to secure their advances or sales.

A major problem confronting our economy today is how what were formally labor-intensive industries may be effectively converted to technologically efficient producers of goods and services. It is in precisely those industries where the impact of S.548 is greatest. The only way such companies may reorganize in Chapter 11 is if, with careful court and creditor oversight, they are able to preserve a sufficient cash and customer base during the Chapter 11 period to enable them to function on at least a break-even basis, while restructing in ways that might permit them to operate profitably in the future. If the effect of S.548 is that all retiree benefits must be paid "off the top", few of those companies would be able to continue in Chapter 11. The choice is not between a Chapter 11 debtor which pays full retiree benefits or a Chapter 11 debtor which does not: the choice is between a Chapter 11 debtor with a prospect for reorganization or a debtor in liquidation. At the present time, unsecured creditors generally fight to keep the Chapter 11 debtor in operation if there is a prospect that the reorganized debtor will be able to pay a greater portion of their claims. If one effect of remaining in Chapter 11 is the diversion of major portions of the debtor's cash to pay the pre-petition obligations due retired employees, the unsecured creditors will almost inevitably join with the secured creditors in their attempts to promptly convert proposed Chapter 11 debtors to liquidation cases. There would be no significant benefit to retirees under those circumstances. S.548 functions only in active Chapter 11 cases. The losers in that context will be not only the retirees, but the current employees and all others who wish ailing entities to reorganize and remain in business.

The principal alternative to reorganization is a liquidation marked by a sale of the assets, free of all liens and encumbrances, to a previously unaffiliated purchaser. The proceeds from such a sale -- almost always far less than the going concern value of the business -- are then distributed, first to lenders who are secured in those assets, and then to other creditors in accordance with the priorities set forth in the Bankruptcy Code. When that happens, the provisions of Section 1113 and the proposed Section 1114 of the Bankruptcy Code will not come into play.

Senate Bill 548 does a number of questionable things. It elevates medical and disability retiree claims which arise out of pre-petition contracts to "cost of administration" (first priority) status, but only those which come due during the post-petition Chapter 11 period. It removes the one-year damages limitation of 502(b)(7) from pension claims of retirees covered by collective bargaining agreements, but not for pension claims of retirees not covered by collective bargaining agreements -- thus distinguishing between union and non-union retirees. It removes the one-year damage limitation of 502(b)(7) from medical and disability claims which arise under plans or programs, but not from those which arise under individual employment contracts. It makes unions presumptively the authorized representatives of retirees; disregarding the inherent conflict between those bargaining for the day-to-day survival of current jobs and a more distant interest. It gives a separate vote on reorganization plans to a retiree class, regardless of size or circumstance, thus increasing the likelihood of expensive and time-consuming "cram-down" battles. It creates a hearing process for retiree benefits with an almost impossible standard to comprehend and apply at an early stage of a Chapter 11 case: that the modification is necessary to permit reorganization, assures that all parties are "treated fairly and equitably", and that the "balance of the equities clearly favors" modification of the retiree benefits. Just how one determines at the onset of a Chapter 11 case what will be necessary to permit reorganization, and how one balances equities before the claims process determines what the equities shall be, or how one "balances equities" to arrive at a solution which "clearly favors", is not detailed. What is assured is uncertainty and extended litigation.

The almost certain result if S.548 is enacted would be to require any debtor contemplating Chapter 11 to move promptly under the proposed Sections 1113 and 1114 to reduce retiree benefits at the inception of a case in which any substantial retiree benefits appear. Failure to limit those obligations would obligate a debtor to pay so much in administrative claims that reorganization would become virtually impossible. To a significant degree, the proposed legislation would require Bankruptcy Courts to determine at the inception of the case whether reorganization is feasible, rather than deferring that determination to the confirmation process or to other later hearings as developed in bankruptcy practice over the years.

One may also express serious reservations about the constitutionality of the proposed legislation. By its terms, S.548 applies to cases and to obligations entered into prior to the enactment. Even if applied only to future cases, it will apply to obligations incurred prior to the enactment, jeopardizing the collateral available to secured lenders and the equality of distribution otherwise existing for unsecured lenders. In effect, the proposed legislation would constitute a "taking" in favor of almost unlimited distributions to one class of pre-petition creditor, while impairing the position of most other creditors.

The ABA Corporation, Banking and Business Law Section, and particularly its Bankruptcy Committee and Chapter 11 Subcommittee, stand ready to make available the expertise of those who work in the debtor reorganization field and their substantial experience to aid the Congress and its staffs in fashioning workable legislation. The speed with which the current proposal has moved has rendered it impossible for those entities to propose alternatives. but we would expect that individuals and various organizations are currently at work on such proposals. We urge most strongly that Congress defer acting on the "quick fix" presented by legislation like S.548. It fails the most simple tests. It is ill-conceived. It will not further the goals it purports to reach. It threatens the utility of a process which does work.

## ANSWERS OF NATHAN B. FEINSTEIN

1. You indicate in your testimony that there are other workable alternatives outside the bankruptcy field to protect the rights of retired employees. I realize at this time it is impossible to discuss specific proposals, but would you discuss generally what other avenues may be available?

With respect to the "retiree benefits" [defined in proposed Section 1114(a) of S.548], the answer would seem to be a requirement for adequate funding during the period of employment of the person who is to become a retired employee of the benefits due after the period of employment. Essentially those benefits are insurance benefits. Insurance actuaries should have little difficulty in determining the current payments required to fund the combination of anticipated benefit obligations and annuity requirements necessary to provide a fund at the anticipated employee retirement date sufficient to pay the medical, surgical, or hospital care benefits portion of the retiree benefits from the date of retirement through the number of years covered by the program or through the retiree's actuarially determined date of death. With respect to the disability or death benefits portion of the "retiree benefits", group disability or death insurance programs abound.

The problem, of course, is that funding such benefits during the period of employment may be expensive, and both the employers and the bargaining representatives would generally prefer to "hock the future" than to provide for realistic current funding. It is easier for the bargaining representatives on both sides of the table (or for the employer-promissor in a non-bargaining situation) to assuage the employee's retirement benefit concerns with a vague promise than it is to earmark a portion of the enterprise's current income for this purpose. Effectively, the promise is often an empty one, and that misleading promise lies at the root of the problem. Probably such empty promises should be prohibited, or there should be a requirement of adequate disclosure to make clear to the employees that the promise may become partly meaningless if the enterprise does not flourish in the future.

To the extent that the promise is unfunded, effectively it is a promise linked to the future economic success of the enterprise: in effect, a kind of equity interest in the enterprise. Accordingly, unfunded benefits should--in theory at least --be considered as inferior in right of payment [see Code Section 510(b), for example], rather than superior as provided in S.548.

If the Congress were really serious about encouraging fully funded "retiree benefits", it could do so by a combination of tax incentives and analogues to the PBGC or social security programs.

The point is, of course, that by linking special retiree benefit legislation to Chapter 11 events, S.548 "funds" retiree benefits at the time the enterprise is weakest and out of the funds required for the entity's survival, rather than when the enterprise is strong and when the promises are made.

2. Your testimony raises a potential conflict of interest question by allowing the exclusive collective bargaining representative of the employees to serve as the authorized representative of the retired employees. Does this legislation not negate the concern raised by the court In Re Century Brass by allowing the union to elect not to serve?

No, it does not. If anything, it exacerbates the concern.

Proposed Subsection (i) to Section 1113 provides that the collective bargaining representative makes the election of whether or not to serve as the authorized representative of the retirees. Thus, the labor organization, in most instances, whose primary concern should be the continued employment and living wage of the current employees, is placed in the exclusive position of bargaining to determine what portion of the scarce assets of the Chapter 11 debtor should be devoted to maintaining current jobs and what portion should be devoted to retirees no longer in the work force (and possibly no longer paying labor organization dues). While unquestionably most labor organizations will be responsible in exercising this choice--and indeed there are strong historic and social considerations requiring them to deal fairly with the retirees--the conflict is not avoided by the legislation. If the labor organization surrenders the right to serve as authorized representative of the retirees, it sets in motion the appointment of a new representative whose interest will be patently adverse to the current employees: thus, the election not to represent the retirees is in effect a determination contrary to the interest of the current employees.

3. You indicate that the standard for confirming the plan for retired employees would be almost impossible to comprehend. Is it the standard itself or the timing in the process which causes the concern?

My comment respecting a standard which would be "almost impossible to comprehend" pertained to the modification provisions of proposed Section 1114(d) and (e), although a similar comment would apply to the confirmation or "cram-down" provision of proposed Section 1129(b)(2)(C)(ii).

With respect to the modification provisions, both the standard and the timing of its application create serious concerns. If S.548 were enacted, it is virtually certain that any careful practitioner representing a debtor would be forced at the inception of the case to move for relief under Section 1114 to avoid a staggering build-up in costs of administration. If debtor's counsel failed to do so, counsel for the secured and unsecured creditors would almost certainly press for such a hearing. The first part of the standard under proposed Section 1114(e) and (f) is that the modifications "are necessary to permit the reorganization of the debtor". That assumes that the debtor already knows what actions will be necessary to permit a reorganization to take place. In any large or complex enterprise, one of the questions explored during Chapter 11 is: Should all of the plants or operations of the debtor be retained? Assuming a disposition of a portion of the debtor's plants or operations, the next question is how much that disposition will bring into the estate as assets useable in funding a plan of reorganization. A related question is the extent of the liabilities (claims) which will be incurred as a result of any such disposition. If there are requirements or other contracts which will not be fully performed because of the disposition, for example, the estate will have a liability for the damages incurred by the breach (rejection) of those contracts. Some evaluation of all of those uncertainties must be made before one can realistically determine what is likely to be "necessary to permit the reorganization of the debtor". At the inception of the Chapter 11 case, since neither the factual underpinnings nor other elements necessary to make those determinations would ordinarily be available, the Section 1114 modification litigation will be almost certain to involve a long and costly battle of expert witnesses making guesses as to future events. At least one appellate court has avoided that part of the problem by interpreting the words to mean the even more rigorous standard of "necessary to the survival of the debtor in order to reach the point where a plan may be proposed". So rigorous a standard is almost certain to be self-defeating. If survival is the test, the debtor would be unable to replenish its capital or fund its operations beyond the survival level, thus rendering reorganization (except by sale to an outside party) almost impossible.

The second part of the test is even more difficult to comprehend or meet. Before one may "assure that all creditors, the debtor, and all of the effected parties are treated fairly and equitably", one must identify all of those parties and evaluate their claims or positions. That is often a long and difficult process, sometimes requiring the completion of major litigation, or as in the case of Robins and Manville, an assessment of thousands of unliquidated claims. Even if those items could be evaluated early in the case, the standard itself creates an almost impossible test: namely, "the balance of the equities clearly favors the" modification. If the equities are truly balanced, how can they "clearly favor" one result or the other? Assume the simplest case: a debtor with sufficient cash flow to just pay a reasonable living wage to the current employees and to pay for the raw materials it needs to continue in business at a break-even level. How is that to be balanced against retiree benefits? If the choice is between shutting down the operations or continuing to pay some part of the retiree benefits, how does one then reach the "clearly favors" position? How does one then balance those scales when there are the additional factors of secured creditors whose collateral is depreciating, providers of services whose claims are growing as additional costs of administration, tax payments or the deferral thereof, etc.

A like conundrum exists with respect to the "cram-down" provision of proposed Section 1129(b)(2)(C)(ii). Assume that virtually all other creditors, including perhaps secured creditors agree to receive something less than the full amount they would be entitled to under the "fair and equitable" and similar plan confirmation standards. What does "consistent with the ability of the debtor to provide such retiree benefits after confirmation" mean? Does it mean that the retirees will be paid out over six years as would the Internal Revenue Service, or does it mean that the retirees will suffer a reduction equal to the reduction which may be agreed to by the secured creditors, or does it mean that the retirees will share the loss equally with the unsecured creditors, or does it mean that the retirees will be forced to accept an empty promise similar to the empty promise they had prior to the filing of the Chapter 11 petition?

The point of all this is that litigation and appeals at virtually every step are a certainty. The debtor or any other party will not be able to "fix" numbers for the retiree benefits during the plan negotiation stage so as to determine what might work in bringing about a feasible plan of reorganization.

Even worse, of course, is the standard contained in proposed Section 1129(b)(2)(C)(i). "Claim" in bankruptcy terminology includes the entire amount of both the matured and unmatured retiree benefit obligation. What this standard seems to comprehend, therefore, is that what was previously an unfunded obligation payable out of each year's earnings, would be required under this subsection of the proposed legislation to become a fully funded plan on the effective date of the reorganization. The legislation would, therefore, place the retirees in a position so far superior to the position they were in pre-petition that no other party in the Chapter 11 proceeding would ever agree to a plan of reorganization that was so inequitable.

The bottom line is that it would be hard to conceive of standards which are more uncertain. It is almost as if the drafters of these provisions intended that they would be so uncertain as to force the debtor in every instance to assume the retiree benefit obligations in the Chapter 11 proceedings. One fears, however, that if that were the intention, it will be effectively thwarted. Debtors and the other "parties in interest" will seek alternatives other than Chapter 11: generally, those alternatives would be immediate liquidation or immediate sale of the debtor's assets, free of liens and claims.

4. If requiring the debtor to pay medical and insurance benefits as an administrative expense between the time of filing the petition for bankruptcy and confirmation of the plan will hinder the debtors' ability to reorganize, how can you insure that the retired employees will receive payment, if not as an administrative expense?

There is no way to "insure" that retired employees or anyone else will receive payment. Designating a particular charge as an administrative expense merely creates a class of priority; it does not speak to the time of payment. Professional persons rendering services to the debtor, and many parties under contract to the debtor, may have their right to be paid as a cost of administration accrue during the Chapter 11 proceedings until a later time (often the effective date of a plan) when the court orders payment. The Second Circuit holdings in the two Flagstaff Foodservice cases, 739 F.2d 73 (2d Cir. 1984) and 762 F.2d 10 (2d Cir. 1985) held that, where a non-consenting secured party remains unpaid, it will be paid prior to costs of administration. Even if Flagstaff were not applied in a given case, if the aggregate costs of administration are greater than the amount available for payment, payment of all such costs would be only pro rata.

Simply calling things "costs of administration" does not assure that they will be paid. What it probably assures is that other creditors, and especially secured creditors, will press for liquidation under Chapter 7 or other forms of liquidation rather than permitting the debtor's assets to be diverted.

5. How do you interpret Section 114(h) on Page 6 of this legislation dealing with offsetting payments of medical and health insurance benefits to retirees?

It provides for a double payment of retiree benefits in the event a plan is confirmed. It virtually assures that no other creditor group will stand by and agree to a plan if a substantial amount is involved in view of the manifest unfairness of the proposed provision.

1. You have expressed a concern in your testimony which, frankly, I share: that is, whether a Chapter 11 reorganization proceeding is or is not the appropriate place to seek the protection of retiree benefits. If it is not, then Congress must find some alternate vehicle for assuring this protection. What suggestions could you make in this regard?

Same as No. 1 above.

2. This legislation would designate payment of retiree benefits due after the date of filing the petition and before the

plan is confirmed as "allowed administrative expenses". In your testimony, you have pointed out the inherent danger in terms of its effect on the ability of the company to reorganize successfully. Could you elucidate on that point?

The "allowed administrative expense" provisions of S.548 would almost certainly have the following effects:

(a) It would cause a severe, and generally fatal, diversion of cash to the payment of a single pre-petition contractual obligation, at the very time such cash is required to keep the debtor alive.

(b) It would make post-petition financing difficult or impossible.

(c) In any case where the cost of retiree benefits is significant, it would dictate that liquidation under Chapter 7 or under state law would be a preferable technique for dealing with the assets. One would find, for example, that a sale of the assets to a third party early in the case would be a preferred method of "keeping the operations alive", leaving the retirees and all other creditors with a fixed fund to which they might look for satisfaction. Since the debtor would not have been able to get its house in order prior to such a "quick sale", the proceeds available for distribution to all creditor classes would generally be minimized.

(d) What Chapter 11 does best is that it requires parties to compromise. By creating one class (the "retirees") which benefits by keeping the case going as long as possible (thus building up the administrative expense payments), and by entrenching a likelihood of payment to that one class, the proposed legislation creates a negotiating climate under which all other creditors would almost certainly refuse to compromise or permit the debtor to continue operations for the benefit of that one preferred class.

(e) It will probably eliminate the use of Chapter 11 in labor-intensive industries, where it is seriously required at the present time.

(f) It creates a priority for retirees in preference to most or all other classes of creditors. In the case of Robins, for example, it assures payment to those people who created and marketed interuterine devices, while limiting the funds available to payment to the women who were the victims of toxic tort resulting from the use of those devices. The same could be said in even greater degree with respect to John Manville, and in any case where tort claims or warranty obligations are a principal factor. To some degree, the same may be true with respect to the cases involving environmental claims.

3. If this legislation were to pass with the provision which elevates the status of retiree benefits to administrative expenses during the pendency of the petition, are there other rights which should receive consideration for similar treatment?

Almost any favored group could be sought out for similar treatment, presumably if they have the political power to effect the goal. Environmental claims, tax claims, Congressmen and Federal officials, members of the right political party, and almost any other type of claim or person has probably received such preference in one bankruptcy system or another. The fact that we have not done so in the United States is a principal reason why the reorganization process works in this country and does not work in almost every other.

1. **Under current bankruptcy law, various parties may wish to extend credit to a debtor-in-possession, after the debtor company files its bankruptcy petition. The Code contains**

some incentives, such as the "administrative priority" under Section 503, so that lenders and other creditors can help the business get back on its feet. Would you agree that one of the needs of any debtor in Chapter 11 is access to new credit?

Post-petition financing is almost always critical to a Chapter 11 debtor.

2. If, under S.548, we now add an additional level of claimants who will get administrative priority treatment, what does this do to the order of payment to those who provide new credit?

S.548 would impede such financing in the following ways:

(a) Virtually no lender in a shakey credit will be willing to see a significant portion of the cash flow diverted to the payment of expenses which do not produce new income. While lenders will agree to lend for the purpose of acquiring raw materials and paying for the labor costs to turn those materials into readily saleable product, thus generating accounts receivable which should turn into cash to repay the loan and help finance increased production, it is hard to imagine an institutional investor agreeing to substantial payments for imprudent or underfunded pre-petition contractual obligations which do not themselves produce cash or saleable assets.

(b) Effectively it would eliminate Section 364(a) and 364(b) as useable borrowing provisions. Post-petition financing would almost always be limited to Section 364(c) super priority or Section 364(d) "Priming Lien" financing. Even under Sections 364(c) and (d), the proceeding to authorize such borrowings would create a hostile environment since the newly created retiree benefit class would be likely to battle superpriority or priming lien financing which would effectively reduce the priority position of that favored retiree class.

3. Accordingly, does adding this class of claimants discourage the continued flow of credit to the debtor, particularly when the debtor may need it most?

Almost certainly. What's worse, the creation of a substantial new class of administrative priority will most seriously impede pre-petition lending to weakened borrowers because of the threat of a substantial diversion of funds available to the Chapter 11 debtor in the event a Chapter 11 petition needs be filed. Even as to a healthy pre-petition borrower, a side effect of S.548 is likely to be the insistance by well-advised lenders that the borrower covenant not to enter into any retiree benefit plan, or at least not to enter into a retiree benefit plan which is not fully funded on a "pay as you go" basis. In the case of "retiree benefits", that will probably mean requiring fully-insured or similar expensive plans.

4. With respect to the concept of equality of distribution under the Bankruptcy Code, does S.548 suggest that some unsecured parties are "more equal" than others?

See response to Senator Thurman's Question 3 above.

5. In your opinion, how have the so-called "Bildisco" procedures set out in Section 1113 worked to date?

Generally they have not. In the Wheeling-Pittsburgh Steel case, it was the strike which realistically settled the labor problem, not the determination of the Bankruptcy Court or the several Appellate Courts. Indeed, the uncertainty caused by the virtually unworkable Bildisco standard almost insured that the provisions would not work, especially after the appellate decision in the Third Circuit.

What is required in labor-management relations following a Chapter 11 petition is relative certainty. Bildisco virtually insures uncertainty, unless by agreement. Probably the most devastating post-petition event is a strike. The debtor's primary post-petition problem is to assure its customers that the flow of goods and services will continue unimpeded, and to assure its 'suppliers that they will be paid. A strike is generally counter-productive. When a strike occurs because the legislative standard is so uncertain that trial court judicial results are unlikely to be accepted by one or the other party, the legislative standard becomes part of the disease.

Senator HEFLIN. The next panel is Mr. Robert G. Watts, executive vice president, A. H. Robins Co., and Dr. Victor Hurst of the AARP, American Association of Retired Persons, of Clemson, SC.

Mr. Watts, if you would, begin.

## STATEMENTS OF A PANEL CONSISTING OF ROBERT G. WATTS, EXECUTIVE VICE PRESIDENT, A. H. ROBINS CO., RICHMOND, VA; AND DR. VICTOR HURST, AMERICAN ASSOCIATION OF RETIRED PERSONS, RICHMOND, VA

Mr. WATTS. Thank you, Mr. Chairman.

In respect of your time and the time constraints of 5 minutes, I am going to forego the written text that we have already given you, and speak to——

Senator HEFLIN. It will be entered in the record.

Mr. WATTS. I appreciate that very much.

I would like to speak to several issues that you may not even find in writing. No. 1, we disagree strongly with the previous witness in that the sense of urgency is not necessary to find a way to save these retirees.

I am the executive vice president of A. H. Robins Co. It has been stated before that we are under the protection of chapter 11 because of a massive tort liability situation. But we are a very profitable operating company. We had sales of $790 million and a profit of $170 million in 1986.

It was ludicrous, incredulous to us when counsel, so-called expert counsel, advised us that we had to file a motion to reject the contracts that covered the benefits of our retirees, whose cost, annual cost for those particular benefits was less than one-half of the monthly fee that we presently pay the attorneys in this bankruptcy case. That means for 20 years we could afford to pay for retirees' benefits what we have already paid lawyers since August 1985.

So, as a profitable company, we think it is important that the debtor should have the right to petition the court to continue the payment and that there be some clarity in the law that provides the court the ability to proceed and approve such.

Through the innovation of District Judge Robert Marriage, and U.S. Bankruptcy Judge Shelley, along with our insurance carrier, we have been able to continue paying our retirees medical benefits—not their life insurance benefits—and it was in the nick of time. That is why I disagree with the concern about the sense of urgency. It was in the nick of time that Congress enacted that temporary legislation which gave the court something to hang on to, to say, yes, you can continue to pay those retirees. We feel it is an urgent matter, and we would implore you to move with haste to find a method which a company, seeking to reorganize under chapter 11, would pay the medical and life benefits of those people who have worked so hard in previous years, and now are considered prepetition retirees.

And I will, Mr. Chairman, be ready to receive your questions in writing or at this time if you so desire.

[The following material was submitted for the record:]

### PREPARED STATEMENT OF ROBERT G. WATTS

Mr. Chairman, Members of the Committee, Ladies and Gentlemen: My name is Robert G. Watts. I am an executive vice president of A. H. Robins Co. Robins is a manufacturer of pharmaceutical and consumer products established in 1866 with corporate headquarters in Richmond, Va. The Company has been operating under chapter 11, U.S. Bankruptcy Code, since August 21, 1985. It petitioned for reorganization as a way of bringing the massive litigation stemming from the Dalkon Shield, an intrauterine contraceptive device Robins removed from the market in 1974, to an expeditious and equitable conclusion. Robins is currently shaping a plan of reorganization for submission to the court that will address compensable claims filed by those seeking restitution through the chapter 11 proceedings.

In 1986, Robins' worldwide sales increased 12 percent to $789,895,000 while operating profits rose 18 percent to $170,188,000. These are new highs for the company, which has advanced sales at an 11-percent compound annual rate and increased operating earnings at 20-percent compound annual rate since 1980. This enviable record is attributable to the tireless efforts of Robins' 6,400 employees worldwide.

Upon the advice of bankruptcy counsel, Robins filed a motion on June 24, 1986, seeking authority of the court to terminate certain employee benefit plan coverage for those disabled and retired employees whose active employment ceased prior to the August 21, 1985, petitioning for reorganization. Robins' management was advised by counsel that the terms of Federal bankruptcy law appeared to require that the motion be filed. The motion affected a group of 329 people and involved their coverage under Robins' medical, dental, and group life insurance plans.

I wish to make it perfectly clear that the filing of the motion was and is repugnant to Robins' management. The motion is contrary to Robins past and present corporate employee relations policy. Robins' management has established an outstanding reputation for fair treatment of its employees. Robins' management has communicated to its retired, disabled and active employees that it did not want to file this motion. The act of filing the motion was taken only because of counsel's advise as to the requirements of those statutes enacted by the Congress. Indeed, Robins business judgment was that medical, dental, and group life insurance coverage could continue for these retired and disabled employees and that the cost of continuing this coverage would not materially affect the ability for legitimate claims in the chapter 11 proceedings to be fairly and equitably addressed.

Our management position today is the same as the day the motion to terminate these benefits was filed. That position is that we are appalled that the law appears to require such an inhumane act be perpetrated on those who unselfishly gave their best employment years to Robins.

Upon filing the motion, the impact was immediate upon the morale of those who were retired and disabled. Also affected were surviving spouses of deceased, retired employees. The effect spread to Robins currently active employees who were shocked that such a motion was required by law, and morale plummeted. The Richmond community responded with letters to management and letters to the editors of our newspapers expressing dismay that Federal law requires retired and disabled people to lose their benefits. Our current workforce responded by joining together to make voluntary donations to defray the legal expenses these retired and disabled employees were incurring while seeking to protect their rights in court. Robins efforts to attract and retain high-quality employees has undoubtedly been affected as potential candidates question whether we can remain competitive in the job market.

This company has an outstanding line of products. Our most important resource, however, is our base of loyal employees. It is essential in any chapter 11 proceeding that management be able to execute those business decisions necessary to retain and attract quality employees. Erosion of a company's human resource asset quickly depletes that company's ability to satisfactorily resolve the issues in any chapter 11 proceeding.

The Congress has enacted temporary legislation which permits companies seeking reorganization under chapter 11, U.S. Bankruptcy Code, to continue benefit coverage for retired and disabled employees through May 15, 1987. When this temporary legislation expires, there currently is no clear and final answer as to whether or not benefits may continue for retired and disabled employees whose active employment ceased prior to the date of filing of a petition under chapter 11.

We urge that Federal legislation be enacted which will provide the latitude for the management of a company which has filed for reorganization under the Bankruptcy Code to make a business judgment decision in regard to continuing benefit plan coverage for retired employees, disabled employees and their eligible dependents. The legislation should recognize that management's decision must take into account what effect continuing the coverage will have on its ability to fairly and equitably address the creditors' claims.

This committee has received testimony directly from those who have been affected by their benefits being stopped. Very basic human needs go wanting when this occurs. I sincerely hope this Nation will express that its national policy is to not allow reorganization proceedings to interfere with a business decision to continue medical, dental, and life insurance benefit plans for retired and disabled employees.

I thank you for allowing me this opportunity to testify. I will be happy to address any questions the committee members may have.

Robert G. Watts
Executive Vice President

A. H. Robins Company
1407 Cummings Drive
Richmond, Virginia 23220
Telephone (804) 257-2251

A·H·ROBINS

The Honorable Howell Heflin
Chairman
Subcommittee on Courts and
Administrative Practices
Committee on the Judiciary
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman: April 14, 1987

Thank you for your letter of April 7, 1987. In response to the supplemental questions which have been posed, we offer the following answers:

Question 1: "Mr. Watts, you testified that A. H. Robins wanted to continue payments to its retired employees. Why didn't the Company then seek court approval to continue the payments in June of 1986 as opposed to asking the court to terminate those payments?"

Answer: The subject of pre-petition retiree benefits was provided an open, thorough and frank debate between A. H. Robins' management and outside bankruptcy counsel. Management took the position that a motion should be filed seeking the Court's authority to continue the medical, dental and group life coverage for the pre-petition retired and disabled employees. It was management's business judgment that filing this "affirmative action" motion would properly bring the issue to the Court's attention and would also ensure equitable treatment of all the parties to Robins' Chapter 11 proceedings. Also, management stressed that this affirmative action position would support Robins' historical employee relations policies and practices while providing a valuable boost to employee and retiree morale.

Robins' management was shocked when outside counsel concluded that Federal Bankruptcy Law mandated the filing of a motion that would cease premium payments for insurance providing benefit coverage for pre-petition retirees. Our counsel advised that, in their opinion, these retiree benefits flowed from promises or contractual obligations made prior to August 21, 1985 -- the date Robins filed its Chapter 11 petition. They also advised that Federal Bankruptcy Law imposed a fiduciary duty on the Company, as the Debtor-in-Possession, to seek the Court's authority to cease the benefit payments. Their advice was clear and strong -- the law left the Company no other avenue than to file a negative motion seeking to terminate the retirees' benefits.

| | |
|---|---|
| Question 2: | "Concern has been expressed that paying retirees' medical and insurance costs will prohibit reorganization of the debtor. Does A. H. Robins share this concern?" |
| Answer: | In 1986, the administrative costs of A. H. Robins' Chapter 11 proceedings were $13,640,000. These administrative costs were attributable to the fees charged by the lawyers, investment bankers, consultants and other professionals who have the Court's approval to be involved in the proceedings. One has to wonder what interest these outside experts have in seeing these proceedings end. In contrast, the cost of Robins' retiree benefits for medical, dental and group life coverage in 1986 was $596,000 -- less than 5% of the annual administrative costs. It is clear in Robins' Chapter 11 proceedings that the administrative costs pose a great burden.<br>Additionally, Robins' net earnings for 1986 were $92,000,000. It appears highly unlikely that the payment of a $596,000 premium for retiree benefits would impede the Company's ability to develop a satisfactory plan of reorganization.<br>It is Robins' business judgment that its reorganization efforts will not be financially impacted by continuing to pay its retirees' benefits. |

If additional information or further clarification is needed, please let me know.

Thanks.

Cordially,

Robert G. Watts

Robert G. Watts

RGW/vc

Senator HEFLIN. We will now be glad to hear from Dr. Victor Hurst of the American Association of Retired Persons.

### STATEMENT OF VICTOR HURST

Dr. HURST. Mr. Chairman, I am Victor Hurst from Clemson, SC. I have with me David M. Sirtner, Esq., legislative representative for Federal affairs of AARP.

I represent the American Association of Retired Persons, representing the interests of more than 25 million members, aged 50 and above.

The Association is pleased to testify today in support of S. 548, the Retiree Benefit Security Act of 1987.

AARP believes this bill will provide needed protection for benefits of both union and nonunion retirees at all stages of the bankruptcy proceedings and urges its early passage.

Retirees depend on their health insurance coverage on a day-to-day basis. Having vested their time in a company, and having retired with the expectation of receiving promised benefits, retirees deserve fairer treatment than sudden termination of these benefits.

Arbitrary action by employers to renege on prior promises and contracts, especially where it concerns essential benefits, should not be allowed to continue unchecked under the guise of bankruptcy proceedings. Contrasted with the position of business creditors in bankruptcy proceedings, retirees often have no other options. Many retirees are unable to find health insurance at this stage in their lives. For those lucky enough to find an available insurance policy, too often that insurance is unaffordable.

The fear and harm of lost benefits affects all retirees who have been promised benefits upon which they rely. Sound public policy calls for a clarification of current bankruptcy law. Fairness dictates that retirees be treated fairly in and in good faith by their former employer.

Certain retiree groups will be hit particularly hard by the loss of employer provided health insurance. Older retirees, who are unable to afford medi-gap coverage, or for whom coverage is unavailable, will certainly be subject to potentially huge health cost increases. Older lower income women often dependent on survivor health benefits are especially vulnerable to increasing health costs.

Another particularly vulnerable group is those retirees who are not eligible for Medicare. Many in this group retired early with a promise of a continuation of employer provided health care insurance. Some with preexisting health conditions may find alternative coverage impossible or prohibitively expensive.

Expedited legislation passed last year protected the welfare benefits of retirees from companies in bankruptcy, but only until May 15 of this year. Further legislation is essential to ensure that all retirees are treated fairly in a bankruptcy situation.

AARP believes that the Retiree Benefits Security Act of 1987 will provide needed protection for all retirees in bankruptcy proceedings.

In conclusion, bankruptcy laws should not permit an employer to unilaterally eliminate essential benefits without respecting the rights of the group that relies so heavily on these benefits. And amending the bankruptcy laws regarding retiree welfare benefits, S. 548 restores fairness to the treatment of retirees in the bankruptcy proceeding.

AARP wishes to thank Senator Metzenbaum for his efforts on behalf of retired Americans, and hopes to continue working with this subcommittee to ensure that legitimate social policy goals are recognized in the Bankruptcy Code. In addition, AARP wishes to work also with Congress to address the larger problem of increased protection for retiree health benefits in all circumstances.

Thank you.

Senator HEFLIN. Because of the timeframe I am going to submit my questions in writing and, at the same time, do you care to do so, Senator Metzenbaum?

Senator METZENBAUM. I will do the same.

[The following material was submitted for the record:]

AARP

STATEMENT

OF THE

AMERICAN ASSOCIATION OF RETIRED PERSONS

The American Association of Retired Persons (AARP) is the nation's largest membership organization, representing the interests of 25 million members age 50 and above. The Association is pleased to testify today in support of S. 548, the "Retiree Benefits Security Act of 1987." AARP believes this bill will provide needed protection for benefits of both union and non-union retirees in all stages of the bankruptcy proceeding and urges its early passage.

## THE PROBLEM

### a. INADEQUATE BENEFIT PROTECTION IN BANKRUPTCY

On July 17, 1986, the LTV Steel Corporation filed for reorganization under Chapter 11 of the Bankruptcy Code. The company, in a July 28 letter to retirees and surviving spouses, then suddenly informed over 78,000 retirees that medical and life insurance benefits that had previously been promised would no longer be provided. In essence, LTV unilaterally cut off vital health and life insurance benefits without prior notice or warning.

Retirees depend on their health insurance coverage on a day-to-day basis. Having invested their time in a company, and having retired with the expectation of receiving promised benefits, retirees deserve fairer treatment than sudden termination of these benefits. Arbitrary action by employers to renege on prior promises and contracts made in good faith, especially where it concerns essential benefits, should not be allowed to continue unchecked under the guise of bankruptcy proceedings.

Contrasted with the position of business creditors in bankruptcy proceedings, retirees often have no other options, and their planned reliance on these benefits cannot be easily or quickly remedied. Many retirees are unable to find insurance at this stage in their lives.

For those lucky enough to find an available insurance policy, too often that policy is unaffordable. This is true not only for those who need supplemental coverage to Medicare, but also for the thousands of early retirees who are not eligible for Medicare. Unilateral termination of benefits is especially unfair for those persons who have been enticed to retire early, in part, by the promise of continued health coverage, only to find, subsequently, these retirement benefits pulled out from under them.

The fear and harm of lost benefits affects not just LTV retirees, but all retirees who have been promised benefits they have come to rely upon. Retiree health benefits are not a luxury; they are central to the well being of retired Americans. Sound public policy calls for a clarification of current bankruptcy law. Fairness dictates that retirees be treated equitably and in good faith by their former employer.

## b. HEALTH COSTS FOR RETIREES

### 1. The Role of Employer-Provided Health Benefits

There are gaps in Medicare coverage, particularly its cost-sharing requirements, which have led to the development of private supplemental insurance plans, so-called "Medigap" policies. About 70 percent of Medicare beneficiaries are covered by such plans. Employers often provide fully or partially subsidized Medigap coverage for their retirees.

There is great variability in the depth and scope of coverage provided by Medigap plans. For example, most Medigap plans provide little or no coverage of prescription drugs, balance billing by physicians, dental services, and extended nursing home care. Under most Medigap policies a waiting period exists for pre-existing conditions, leaving the individual liable for all costs related to that condition until the waiting period is over. Even if available, such plans may be too costly relative to the benefit returned to the insured.

Even small increases in health care costs for retirees can force individuals to forego needed care -- or forego other necessities to afford basic health care. The burden increases greatly when employer-provided health insurance is eliminated. In these instances, the increase of medical care costs for individuals can be devastating.

### 2. Those Most Vulnerable When Health Benefits Are Lost

Certain retiree groups will be hit particularly hard by the loss of employer-provided health insurance. Older retirees who are unable to afford Medigap coverage, or for whom coverage is unavailable, will certainly be subject to potentially huge health cost increases. Those who do not qualify for Medicaid, particularly older, frail, lower income women, often dependent on survivor health benefits, are especially vulnerable to the cumulative financial burden of increasing health costs. Already such expenses amount to an average burden of 15 percent of the incomes of persons over age 65. For the very old and the sick, out-of-pocket expenses consume an even larger share of income.

With employer-provided coverage eliminated, and substitutes too expensive, if available, these retirees will be subject to far greater expenses than anticipated, leaving no choice for the retiree to secure alternative coverage.

Another group of great concern are those retirees who are not eligible for Medicare. Many in this group retired early with the promise of the continuation of employer-provided health care insurance. This group is particularly vulnerable if their health insurance is cancelled. They are not eligible for Medicare, and many who thought they would get care through the veterans health care system find that recent changes in eligibility make this option no longer available to them. Again, pre-existing conditions may make alternative coverage impossible, or prohibitively expensive. Retirement planning is impossible, and the lure of early retirement may prove to be an unexpected insurance trap.

## PROPOSED LEGISLATION

Expedited legislation passed last year protected the welfare benefits of retirees of LTV and other companies filing for Chapter 11 bankruptcy, but only until May 15 of this year. Further legislation is thus essential to insure that all retirees are treated fairly in a bankruptcy situation. AARP believes the Retiree Benefits Security Act of 1987 will provide needed protection for retirees in bankruptcy proceedings.

First, the bill would clarify the current interpretation of Section 1113 of the Bankruptcy Code covering collective bargaining agreements to insure that retiree benefits receive the same protection as all other benefits. This will prevent the unilateral termination of retiree benefits by the employer at the time of filing the petition for bankruptcy. (This clarification will prevent a repeat of the LTV situation).

The bill will also deal with the potential conflict-of-interest faced by labor organizations that must represent two groups with often different concerns -- active employees and retirees. Under this legislation, the union has the right to represent retirees if they so choose. If the union decides not to represent the retired employees, the court can intervene and appoint a committee of retirees to represent the group.

Second, this bill does more than simply protect union employees in collectively-bargained cases. This bill extends protection to all retirees -- both union and non-union -- by adding a new section to cover health and life insurance. This section requires the employer to continue paying benefits until a court, after a hearing, orders a change, or unless the representative agent and the employer agree to a modification. By treating these benefits as "administrative claims," the bill insures these benefits will be paid.

The court will order a modification only if it determines that such a change is necessary in order to permit the company to reorganize under the bankruptcy laws. The bill requires that the modification be fair to all creditors, and treat every party fairly and equitably. The court will thus be required to use a balancing test in weighing the equities, and the retirees' concerns must be included in that balance.

Third, the bill will allow the retirees to vote as a separate class in reaching an agreement on a final plan reorganization. This will again insure that retirees have a voice in any final reorganization, and should better protect their benefits in any final plan to get the company out of bankruptcy. While any one class can prevent final plan approval, the refusal to agree must be reasonable. By allowing retired workers to vote as a separate class, reasonable retiree claims to benefits will carry extra weight.

The end result of these changes is better protection of the rights of both union and non-union retirees in all stages of the bankruptcy proceeding. A retired worker will have guarantees of fair treatment, including a day in court, before any modifications to promised benefits are made.

## CONCLUSION

Already burdened by the high cost of health care, older Americans who previously believed they had earned a guarantee for continued employer health coverage are now living with the fear that employer-promised benefits may be terminated. Bankruptcy law should not permit an employer to unilaterally eliminate essential benefits without respecting the rights of the group that relies so heavily on these benefits. In amending the bankruptcy laws regarding retiree welfare benefits, S. 548, the Retiree Benefit Security Act of 1987, restores fairness to the treatment of retirees in the bankruptcy proceeding.

The question of the treatment of retiree health benefits in bankruptcy points to the larger problem of the status of employer-provided retiree health benefits in general. Currently, while many employers offer retiree health benefits, few companies adequately fund these benefits. In addition, the legal status of these benefits is subject to varied judicial and legislative interpretation. While this bill addresses the narrow, but important problem of retiree benefits in bankruptcy, the larger question of increased legal protection for all retiree health benefits has yet to be adequately answered.

AARP wishes to thank Senator Metzenbaum for his efforts on behalf of retired Americans, and hopes to continue working with this Subcommittee to insure that legitimate social policy goals are recognized in the Bankruptcy Code. In addition, AARP wishes to also work with Congress to address the larger problem of increased protection for retiree health benefits in all circumstances.

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AARP

April 29, 1987

Ms. Gail Ludwig:
Subcommitte on Courts and
Administrative Practice
223 Senate Hart Office Building
Washington, DC 20515

Dear Ms. Ludwig:

Attached please find a copy of the follow-up question, with an attached answer, asked by Chairman Heflin for the April 1 hearing on the Retiree Benefits Security Act. The question was addressed to Dr. Victor Hurst.

Thank you in advance for your attention.

Sincerely,

David Certner

David Certner
Legislative Representative

* * *

## RESPONSES OF DR. HURST TO WRITTEN QUESTIONS

### SUBMITTED BY SUBCOMMITTEE

**Q. 1.** When a company terminates a retiree's health and life insurance benefits, the retiree is forced to go out and seek a substitute plan. Isn't it true that retirees often have to settle for health and life insurance coverage which is more expensive and provides less coverage than their former plans?

**A. 1.** You are correct that retirees often have to settle for health and life insurance coverage which is more expensive and frequently provides less coverage when trying to replace the plans offered by their former employees.

We have done a recent search of available data but were unable to locate any specific information detailing the extra out-of-pocket costs incurred because a plan terminates and the retiree must replace a group policy with an individual plan.

Senator **Heflin**. Thank you, gentlemen. We appreciate it.

The next panel is Mr. Richard A. Gitlin and Mr. William Perlstein of the American Bankruptcy Institute.

Mr. Gitlin, we will be delighted to hear from you first.

## STATEMENTS OF A PANEL CONSISTING OF RICHARD A. GITLIN, PRESIDENT, AMERICAN BANKRUPTCY INSTITUTE, AND WILLIAM PERLSTEIN, LEGISLATIVE CHAIRMAN, AMERICAN BANKRUPTCY INSTITUTE

Mr. **Gitlin**. Mr. Chairman, with your permission, I will summarize my comments. We have submitted a written statement.

The American Bankruptcy Institute is a nonpartisan organization designed to help all those interested in the bankruptcy process. Our membership includes more than 1,600 lawyers, judges, accountants, bankers, business leaders, professors and others who are actively involved with the operation of the Nation's bankruptcy laws.

Although I am president of the American Bankruptcy Institute, my comments today are made personally, Mr. Chairman, and not on behalf of the institute.

However, the American Bankruptcy Institute has and will continue to offer whatever services and advice it can to the Senate and to the House on this and other bankruptcy-related topics.

Mr. Chairman, I agree with the drafters of S. 548 that the plight of the retirees is real and tragic. I almost could not join you today because my mother is quite ill. And it probably takes a personal experience to see how people's dignity is challenged when they are elderly and ill. Whether they are part of a retirement plan or part of the Medicare plan, it is very sad to see the way we treat our elderly in this country. We should, with our resources, be able to treat them with greater dignity and respect.

Therefore, I firmly believe that a solution to the problems of those retirees here today, and those who do not have the benefit of retiree plans at all, is essential.

The questions, however, is whether chapter 11 is the appropriate vehicle to provide a solution. Mr. Feinstein went through a number of arguments with respect to chapter 11. I would simply like to make two comments.

I frequenty have occasion to deal with attorneys and bankruptcy laws throughout the world. What I have found in other countries recently is that they are amending their laws to be closer to chapter 11. They discovered that during periods of economic stress that chapter 11 gave us a much better opportunity to restructure our companies. We kept the jobs and they did not. So they are looking at chapter 11 to capture what parts of it they can build into their countries. England recently did this.

There are two key elements of chapter 11. One, give the business a breathing spell and allow it time to build its business base. Once the business is given that opportunity, it will have a chance to recover and will likely have more assets for everybody. The first key element is a breathing spell.

The second key element is the balance of power among the creditor groups that enables them to negotiate a transaction. Any chapter 11 that ends up being litigated is a chapter 11 that spends most of its money for lawyers' fees and other parties, ends up taking longer, and ends up probably less successful. So it is very important to have a balance among the creditor groups so they are encouraged to do an agreement that is in everyone's interests.

So, on the one hand, chapter 11 offers the ability to rehabilitate the asset base and, on the other hand, provides a balance of power so that a consensual agreement will be reached. To the extent you impair those two elements, you impair the vitality of chapter 11.

There are few chapter 11's that do not involve tragic results. I can think back in every chapter 11 that I have been involved with, and someone has been tragically hurt, whether it is the debtor's supplier who has built his business all his life only to go under because the debtor cannot pay its bills; whether it is the people who have been injured by a product, and their injury and pain and suffering does not go away; yet despite the misery that chapter 11 brings to these people, such misery is a necessary byproduct in order for chapter 11 to accomplish its goals.

No one wants misery to anyone; that is not chapter 11's purpose. But hopefully, and I think it has worked in the past, chapter 11 can be used to make a bigger base for everybody and, frankly, preserve jobs.

Our concern about S. 548 is that it impinges on the two key elements of a breathing spell and creditor balance, may harm the very business and jobs that chapter 11 strives to protect, and may, in fact, hurt the very retirees that are trying to help.

I fully endorse the principle of Mr. Williams. If we can find a nonbankruptcy solution, however, whether it is PBGC solution, an insurance solution, or whether we will have done ourselves a great service. We will preserve benefits for these people who desperately need them while, at the same time, companies in trouble can rehabilitate and save jobs, and preserve more for the retirees in the end.

In our written testimony, however, we recognized that a nonbankruptcy solution may not be immediately available. The reality is we have people injured today. We have people who need health benefits today. Therefore, we suggested a few alternatives in our written testimony which do not go as far as S. 548, but still deal with the crisis that is before us. Mr. Chairman, we strongly urge that the Senate consider those solutions and the other solutions suggested to you today.

Finally, Mr. Chairman, while the committee is considering those possible solutions and the other nonbankruptcy alternatives that have been suggested today, we would ask for your committee to entertain an extension of the temporary legislation. Keep the protective shell over the people who are being injured while we struggle a little bit harder to try and find a solution that satisfies the crying needs of the people you are trying to protect while, at the same time, preserves the vitality of a chapter 11 to rehabilitate a business.

[Statement of Mr. Gitlin follows:]

Testimony of
Richard A. Gitlin
President, American Bankruptcy Institute

Concerning S.548

On behalf of the American Bankruptcy Institute, I extend our sincere appreciation to the Chairman and the Members of the Subcommittee for the opportunity to appear before you to discuss S.548. With me is William J. Perlstein of Washington, D.C., who is chairman of the ABI's Legislation Committee. The American Bankruptcy Institute is a nonpartisan membership organization of more than 1,600 lawyers, judges, accountants, bankers, business leaders, professors and others who are actively involved with the operation of the nation's bankruptcy laws. While we appear before you as representatives of the ABI, the views we express are necessarily our own and do not represent the official view of ABI.

## I. The Plight of Retired Workers

An employee works for a company for ten, twenty, thirty or more years. As part of the employment relationship, the employer agrees to provide for the employee and his or her spouse and dependents health, disability and death benefits for the years after the employee retires. Such benefits can provide substantial assistance to a number of families, and in many cases, are irreplaceable. The plight of retired workers of an insolvent company is very real.

As demonstrated by several recent bankruptcy filings, Chapter 11 of the Bankruptcy Code does not address the plight of retired workers. Congress responded to the problem by mandating the continuation of retiree benefits through May 15, 1987, and we agree with Congress that further protective legislation is needed to safeguard retiree benefits after the emergency legislation expires.

While we agree with the goals of the drafters of S.548, however, we must respectfully disagree with the methods by which S.548 proposes to reach those goals. It is our gravest concern that S.548, rather than creating a Chapter 11 cure for the plight of retired workers, will instead result in more harm than good being done.

## II. The Chapter 11 Process

Chapter 11 of the United States Bankruptcy Code is a statute and a process that can be found nowhere else in the world. In the vast majority of countries, a company that enters bankruptcy is simply liquidated, and often only the secured creditors, the professionals and the government get paid. Under Chapter 11, a financially-troubled enterprise is given a breathing spell -- an opportunity to reorganize.

Shareholders benefit from Chapter 11, because it gives them the opportunity to recoup some of their investment. Trade creditors benefit from Chapter 11, because it gives them the opportunity to recover more on their claims than they would ever receive in a liquidation, and it enables them to continue a trading relationship with a valuable customer. Many of the trade creditors are in financial difficulty themselves, and the loss of a large receivable or customer could well prove ruinous.

Perhaps more than anyone else, employees benefit from Chapter 11. If Chapter 11 were not available to employers, the harms potentially suffered by a company's retirees under the present law (before the enactment of the emergency legislation) might easily be matched or surpassed by the harms suffered by the many more current employees who would be out of a job. In turn, the communities in which those employees work would be damaged, thus spreading the economic misery of the bankruptcy case far beyond the immediate parties in interest. Finally, of course, local, state and federal governments would suffer a significant loss in tax revenues and a substantial increase in expense, thus harming us all.

The Chapter 11 process involves a system of checks and balances designed to protect and promote the interests of all the affected parties. The amount of claims entitled to priority treatment are kept at a minimum in order to free up more funds for the continued operation of the debtor's business and to increase the distribution to the general unsecured creditors. The classification scheme for reorganization plans is precisely tailored to the competing leverage and interests of the various administrative, secured, unsecured and equity claimants. The requirements of Section 1113 ensure that current employees will be treated as fairly as possible within the context of the debtor's financial distress.

Before we add additional protections to Chapter 11 for the benefit of one particular group -- retirees -- we should ensure that such "protections" don't so upset the existing delicate system of checks and balances as to cause a greater harm to all involved, including the very retirees that S.548 is designed to protect.

## III. Some of the Problems with S.548

Our general concern with S.548 is that the bill not only may not achieve the goals for which it is intended, but may harm the whole reorganization process. We believe that the bill as drafted may well result in far more liquidations, far fewer reorganizations, and far greater harm to the very retirees that the bill is designed to protect. While there are many parts of the bill that cause us such concern, there are three particular parts to S.548 that are especially troublesome.

First, the bill imposes potentially massive liabilities on the debtor by characterizing all health and disability benefits payable during the reorganization proceeding as administrative expenses.[1] Under the Bankruptcy Code administrative expenses must be paid in full in cash before a plan of reorganization can be confirmed. For this reason, the courts have limited administrative claim status to those expenses incurred by the trustee or the debtor for post-bankruptcy services benefitting the estate. Retiree expenses do not meet this test since retirees are providing no current services to the estate. Under the proposed bill, however, retiree expenses will accrue as administrative expenses until the Court allows a modification. This will force the debtor to move promptly to seek an order reducing benefits, assuring labor-management discord early in the case.

Moreover, even if the debtor can show irreparable damage, these expenses continue to accrue until the Court makes a final decision on the debtor's motion, which could take months to determine. If the debtor continues to pay the benefits, the bill will deplete the debtor's cash resources early in the case, at a time when the debtor often has its most critical cash needs. In addition, the threat of massive administrative expense liability will discourage current suppliers from extending any credit to the debtor, potentially crippling the debtor's efforts to operate while reorganizing. Paying retiree benefits may well threaten the jobs of all current workers.

Second, the bill establishes retirees as a separate class of creditors in voting on a proposed plan of reorganization. Most plans place all unsecured creditors in a single class. All claimants in the class vote on the plan, and the class accepts the plan if at least two-thirds of the dollar amount of claims and a majority of voting claimants vote to accept it. While the majority thus can bind dissenters, each

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1/ Proposed Section 1114(d)(2).

dissenting creditor is protected by the so-called "best interests" test of the Bankruptcy Code.[2/] That provision requires the Bankruptcy Court to determine that each dissenting creditor will receive at least as much under the plan as it would receive if the debtor were liquidated. The Bankruptcy Code's treatment of unsecured claims is one of the most critical of the checks and balances incorporated into the Chapter 11 process.

The proposed bill would significantly change this procedure for treatment of unsecured claims and threatens to decrease the effectiveness of the Chapter 11 process. The bill would require the creation of a class composed solely of retirees. It seems quite likely that these claimants will vote against any plan, thus necessitating what is known as a "cramdown" to obtain approval of the plan. The cramdown process is the procedure used to obtain confirmation of a plan over the opposition of a class of creditors. It is often a costly and time-consuming process and no plan proponent looks forward to obtaining confirmation using a cramdown. By mandating a separate class for retirees, the bill greatly increases the chances of having to resort to cramdown, delaying confirmation to the detriment of current workers and suppliers.

It is noteworthy that, when current employees' benefits are reduced under Section 1113, their claims are not treated as a separate class and they are included in the general unsecured creditor class. Thus the bill does more for retirees than Congress did for current workers when it adopted Section 1113 in 1984.

Third, the bill establishes an unprecedented standard for utilizing a cramdown for the retiree class. To effect a cramdown on this class either the debtor will have to pay the claimants their claims in full or the Court will have to de-

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[2/] 11 U.S.C. § 1129(a)(7).

termine that the plan offers the retirees the "minimum reduction consistent with the ability of the debtor to provide retiree benefits after confirmation."[3] We are frankly not sure what this provision means. The claims in this class consist of future benefits that the Court has authorized the debtor to withhold following modification of the retirement plan. Even after the debtor obtains a court-approved modification, the bill appears to provide that a reorganization plan can be confirmed only if the debtor agrees to repay the maximum possible amount to such claimants, all the while continuing to pay currently all retiree benefits (possibly at the modified level approved by the court) accruing after confirmation of the plan.

This provision is very troubling. It could be read to bar payments to any other unsecured creditor class if the retiree class is not paid in full. It could also be read to require a reexamination of the provisions of the collective bargaining agreement governing current workers, to see if further cuts could be made there. It certainly will be argued that it bars payments to shareholders in such situations. And at a minimum it will require a second determination of the debtor's ability to pay retiree benefits. Again, current workers have no such protection for lost benefits, nor does any other class of unsecured creditors. One sponsor described this provision as giving the retirees a "veto" over the reorganization process.[4] We agree with this characterization, and we are very troubled by the prospect of such a fundamental change in the bankruptcy laws.

These are only some of our concerns with the proposed bill that illustrate the dangers of special treatment for the retiree class. No other group of creditors, including current employees, receives such unique treatment. Congress artfully crafted the confirmation process in the 1978 Bankruptcy Reform Act to encourage consensual plans by carefully balancing benefits and burdens among secured creditors, unsecured creditors and the debtor. Even when Congress enacted special labor provisions in 1984, it did not alter the plan confirmation process. The current bill is troubling and potentially dangerous in giving to a single group such power to delay or scuttle the confirmation process.

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[3] Proposed Section 1129(b)(2)(C).

[4] 133 Cong. Rec. S.2238 (daily ed. Feb. 19, 1987)(Statement of Mr. Heinz).

## IV. Alternative Solutions

As we indicated at the outset, we concur with the drafters of S.548 that retired employees of a Chapter 11 debtor should not be unfairly forced to suffer the loss of health, disability and death benefits promised to them. The proposed bill, however, while laudable in spirit, may not accomplish what its drafters have in mind. It will may well lead to far more liquidations, and everyone -- retirees, employees, trade creditors, shareholders, society as a whole -- may be worse off, not better. What is called for in reality is a nonbankruptcy solution that will protect retiree benefits, even if an employer is unable to reorganize and winds up liquidating. While S.548 will protect the retirees of the relatively few employers who will be able to reorganize notwithstanding the proposed bill's enormous economic demands, a nonbankruptcy solution will provide protection to the retirees of all financially-troubled employers, whether or not they can reorganize successfully.

If Congress ultimately determines that it must provide a bankruptcy solution to the retiree benefit problem, there are a number of alternative suggestions in the bankruptcy context that would better preserve the existing Chapter-11 process better than S.548.

One suggestion would be to require a debtor to maintain health and disability benefits for retirees for the first 60 days after bankruptcy. This would prevent abrupt termination of such benefits. During that 60 day period retirees would be notified that they would have to pay for their own benefits after that time. The debtor would be required to maintain group policies in effect for each employee who elects to pay the required premium, which would undoubtedly be far less costly than individual coverage. When the debtor was providing such benefits through self-insurance, the debtor would be required to obtain a group policy to be offered to retirees.

This approach serves many of the same objectives as S.548 but without fundamentally altering the reorganization process. It prevents abrupt termination of benefits and offers retirees the opportunity to obtain group policies and rates. The additional cost to the retirees would become an unsecured claim in the case and the retirees would receive payment on their claim on the same terms as current employees and other creditors are paid on their unsecured claims. This approach avoids the uncertainty and turmoil threatened by S.548 and preserves the delicate balance needed for an effective reorganization process. We urge the careful consideration of an approach of this type instead of the administrative claim and cramdown approach of S.548.

A second alternative that adopts part of S.548 but would better serve the rights of all concerned is also possible. This alternative would involve retaining the parts of the proposed bill that amend Section 1113 and add Section 1114 (with certain revisions to clean up several ambiguities and redundancies), but discarding the rest. In that way, retirees would be treated equally with current employees in the administration stage of the Chapter 11, but they would not be preferred over current employees, as well as all other unsecured creditors, at the confirmation stage. Again, we emphasize that our concern isn't that S.548 might permit retirees to come out slightly better than other classes. Rather, we greatly fear that the proposed bill will result in all constituencies, including retirees, faring far worse.

Yet a third alternative may be possible that involves an increase in the allowable amount of retiree priority claims and the maintenance of current retiree benefits at a reduced level. In addition, we have no doubt that there exist other potential alternatives that properly address the plight of retired workers while preserving the viability of the Chapter 11 process, which brings us to our final point.

In our rush to meet the May 15, 1987 deadline imposed by the emergency legislation, we must not let time constraints impose on us a bill such as S.548 that, while well-intentioned, does not appear to further the goals that its drafters have in mind. Instead, we strongly urge that Congress extend the May 15, 1987 deadline for a reasonable period of time, so that these alternative proposals and others can be given the attention they deserve.

Senator HEFLIN. Thank you, sir.
Mr. Perlstein.

## STATEMENT OF WILLIAM PERLSTEIN

Mr. PERLSTEIN. I do not have a separate statement from Mr. Gitlin, Senator Heflin.

I would like to add one thing to what Mr. Gitlin said in response to what Mr. Williams said. Mr. Williams pointed out that many members of the bankruptcy bar did oppose section 1113 in 1984. I was privileged to work with Senator DeConcini, with yourself and others, in 1984 representing the ABA at that time on the bankruptcy legislation. And there were many statements made of the risks that section 1113 posed to the bankruptcy process.

One of the major changes between section 1114 and section 1113 is that section 1113 dealt solely with issues of the claims, the size of the claims, and the rejection of the collective-bargaining agreement. It did not at all amend or revise the confirmation process.

And my major concern, the major concern, that many people looking at this bill have, is that the confirmation process will be changed in a really unprecedented way. The speakers this morning who supported the bill pointed to that. It is of great concern to those of us who have to get chapter 11 plans through from the initial petition through the confirmation process.

Setting up a separate class, saying that if that class opposes the plan, that you have this special cram-down process with unprecedented cram-down procedures, is a major change, changing what Congress had very carefully crafted in 1978 in the balancing that Mr. Gitlin pointed to.

I would urge the members to consult with a broad range of people involved in the process as to what that change risks. I see that risk as having every case, frankly, turning into a Manville. A bankruptcy case should, in most cases, be able to get through from the initial petition through confirmation in 1½ or 2 years, the yardstick that most of us use. If you are beyond that, you are talking about tremendous differences in the time value of money. You are also talking about a tremendous difficulty in getting the company reorganized.

Manville took nearly 5 years and is not done yet because of the appeals. If we set up yet another class, get another cram-down procedure, someone else yet able to block the plan, what you are risking is that every case turns into a Manville. Mr. Watts complained about the legal fees in the *Robins* case. That is what you will be looking to in cases much less complicated than Robins.

Thank you for your time.

Senator HEFLIN. Thank you.

We will submit some questions to you.

[Responses of Messrs. Gitlin and Perlstein, subsequently submitted for the record, follow:]

# ANSWERS OF
# RICHARD A. GITLIN AND WILLIAM PERLSTEIN
# IN RESPONSE TO WRITTEN QUESTIONS RE S. 548

1. Question: You have expressed a concern in your testimony which, frankly, I share; that is, whether a Chapter 11 reorganization proceeding is or is not the appropriate place to seek the protection of retiree benefits. If it is not, then Congress must find some alternate vehicle for assuring this protection. What suggestions could you make in this regard?

Answer: As indicated in our written testimony, we perceive two major problems with attempting to utilize the Chapter 11 process to assure payment of retiree benefits. First, the additional layer of current priority expenses that such funding would cause could damage the delicate Chapter 11 process and lead to more liquidations. Second, requiring the current funding of retiree benefits in a Chapter 11 will only protect those retirees whose employers are able to reorganize successfully. For those retirees whose employers are unable to reorganize successfully, or are otherwise liquidated outside of the bankruptcy court, they will still face the problem of unfunded retiree benefits. Our proposal, therefore, is that Congress seek to implement a non-bankruptcy solution that will provide protection to the retirees of all financially-troubled employers, whether or not they are able to reorganize successfully.

As suggested by our colleague Nathan B. Feinstein in his written response to this same question, one possible non-bankruptcy solution would be a requirement that employers adequately fund on a current basis their anticipated future retiree benefit obligations. It should be relatively simple on an actuarial basis to determine the level of current payments required, and the employer should certainly be better able to make those payments when it is a healthy going concern than when it is operating in a Chapter 11. Along the same lines, employers could be required to maintain private insurance sufficient to cover all vested retiree benefits.

As a supplement or alternative to the foregoing privately-funded solutions, Congress should also consider the creation of a public retiree benefit support system, such as the system in place with respect to pension benefits.

We recognize, of course, that implementation of any of the above non-bankruptcy solutions will require a significant private or public economic investment. Nevertheless, if the goal is to protect the benefits of retirees of all financially-troubled employers, and not simply the retirees of those employers able to reorganize successfully under Chapter 11, then such non-bankruptcy solutions will better address that goal.

2. Question: This legislation would designate payment of retiree benefits due after the date of filing of the petition and before the plan is confirmed as "allowed administrative expenses." In your testimony, you have pointed out the inherent danger in terms of its effect on the ability of the company to reorganize successfully. Could you elucidate on that point?

Answer: Generally speaking a Chapter 11 debtor has a relatively fixed amount of postpetition cash flow with which it must satisfy a variety of obligations. Those obligations typically include current operating expenses, taxes, court-related expenses, payments to secured creditors, and adequate protection payments. By designating payment of retiree benefits as an additional "allowed administrative expense," S. 548 would substantially increase the amount of postpetition obligations that the debtor would be required to pay currently, while leaving the postpetition cash flow at the same fixed level. As with any business in or out of bankruptcy, when current income remains constant but current expenses increase, there is a danger that the business will not survive.

For a relatively healthy Chapter 11 debtor, current payment of retiree benefits, while inevitably reducing the cushion between postpetition cash flow and postpetition administrative expenses, should not fatally affect the debtor's reorganization prospects absent an economic downturn. For relatively weak Chapter 11 debtors, on the other hand, it is easy to envision that the additional layer of administrative expense will simply make it impossible for the debtor to reorganize. For the large number of Chapter 11 debtors that fall somewhere in between, a new administrative expense for retiree benefits will make it that much more difficult for them to reorganize. The designation as an administrative expense will require some employers to move quickly to reduce these benefits in order to preserve cash flow. In other cases the mandating of the payment of retiree benefits will require the employer to move to reduce the wages of current employees. In many such cases, we fear that these added expenses could prove to be more than the debtor can handle.

3. Question: If this legislation were to pass with the provision which elevates the status of retiree benefits to administrative expenses during the pendency of the petition, are there other rights which should receive consideration for similar treatment?

Answer: As we indicated in our written testimony, we agree with the drafters of S. 548 that retired employees of financially-troubled employers merit protection of their retiree benefits. However, there are many other individuals and entities (such as tort victims, certain trade suppliers, pensioners, and current employees whose wages and benefits are reduced pursuant to Bankruptcy Code § 1113, to give four examples) who are probably deserving of some protection for particular benefits or obligations due them. It is quite evident, however, that if all claims as deserving of administrative status as retiree benefits received special priority treatment, the Chapter 11 process as we know it would no longer be viable.

1. Question: You indicate in your testimony that there are other workable alternatives outside of the bankruptcy field to protect the rights of retired employees. I realize at this time it is impossible to discuss specific proposals, but would you discuss generally what other avenues may be available?

Answer: See answer to Question No. 1 above.

**Senator Heflin.** I want to thank the American Bankruptcy Institute for their cooperation in accommodating the needs of the subcommittee because we do need to expedite this matter.

You, I understand, may want some additional time and between now and the 24th, if you have additional thoughts, we would be delighted to receive those thoughts. You can submit them by either writing or a mixture of oral and written submission.

So, with that, we will conclude the hearing, and thank you very much.

[Whereupon, at 12:35 p.m., the subcommittee adjourned, subject to the call of the Chair.]

# RETIREE BENEFITS SECURITY ACT OF 1987

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FRIDAY, APRIL 24, 1987

U.S. Senate,
Subcommittee on Courts and Administrative Practice,
Committee on the Judiciary,
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10:05 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Howell Heflin (chairman of the subcommittee) presiding.

Also present: Senator Metzenbaum.

## OPENING STATEMENT OF HON. HOWELL HEFLIN, A U.S. SENATOR FROM THE STATE OF ALABAMA

Senator **Heflin**. The subcommittee will come to order.

I would like to welcome to the Courts and Administrative Practice Subcommittee of the Judiciary Committee those testifying today and all those interested in this legislation. Welcome to the second day of hearings on S. 548, the Retiree Benefits Security Act of 1987.

This legislation addresses the problem of retired employees who worked for companies that have subsequently filed for bankruptcy under chapter 11 of the Bankruptcy Code. By chapter 11, we are referring to the section of the Bankruptcy Code that deals with reorganization, not chapter 7 which is outright bankruptcy.

This legislation would amend the bankruptcy laws in an attempt to better protect the medical and insurance benefits of those workers. In the 99th Congress, legislation was passed as a stopgap measure to require companies that went into chapter 11 bankruptcy to continue paying medical and insurance benefits to retired employees through May 15, 1987.

Because of our fears that the May 15 deadline might pass without permanent legislation having been enacted, the Senate passed S. 903 on April 10 of this year, which would extend the May 15 deadline to September 15, 1987. The House of Representatives must now consider the extension measure. We hope that they will expeditiously consider and pass the Senate-passed bill, which would extend this temporary legislation until September 15, in order that a permanent bill can be adequately and comprehensively considered and passed.

All of us realize that this is a very complicated issue and one that demands an expeditious but also a thorough and reasoned response; not one done so quickly that we undo the good that we are trying to accomplish.

Many of my fellow Alabamians were hurt when LTV filed for chapter 11 reorganization in the Bankruptcy Court in July of 1986. Their medical and insurance benefits were terminated. I sympathize with them and many other retirees that have been hurt by chapter 11 bankruptcy filings. No other class of creditors is as vulnerable as retired employees during the bankruptcy process. Their benefits are not luxuries but they are essentials of life.

We have numerous witnesses today; and, in order to accommodate as many witnesses as possible, we will adhere to the 5-minute rule. The 5-minute rule is illustrated by these lights. While 5-minutes is in play, the green light will be on; but at the end of the 5 minutes the red light is on. I suggest that the red light be observed by the witnesses, else their ears might be hurt by the piercing sound of this gavel.

A copy of the written statements of each witness will be placed in the record, and I ask that each witness summarize your testimony. I appreciate your attendance at this hearing and we look forward to moving ahead at this time.

Senator Metzenbaum will be here and will have an opening statement, so we will interrupt when he arrives for him to make his opening statement.

Also, I would like to include in the record statements by Senators Thurmond and Grassley at this point.

[The prepared statements of Senator Thurmond and Senator Grassley follow:]

## PREPARED STATEMENT OF HON. STROM THURMOND, A U.S. SENATOR FROM THE STATE OF SOUTH CAROLINA

Mr. Chairman: I would like to commend the distinguished chairman of the subcommittee, Senator Heflin, for calling this second day of hearings on the Retiree Benefits Security Act. The importance of this hearing is underscored by the chapter 11 filing of Texaco since our last hearing on this matter.

I share concern about the protection of retiree health benefis. I am committed to seeking a fair and equitable solution for all unsecured creditors, including retirees, to the problems they are encountering during the pendency of chapter 11 proceedings.

Nonetheless, I am still troubled about the approach taken in S. 545 to protect retiree benefits. We will receive testimony today which will highlight my concern about seeking protection for retirees through the creation of a statutory priority in chapter 11.

Several questions must be answered about the approach taken in this legislation, such as: What impact will the bill have on the rights of other unsecured creditors who, like retirees, lack the economic leverage to protect claims in bankruptcy cases? What impact will the bill have on the ability of companies to achieve the paramount objective of chapter 11—to reorganize and remain a viable entity?

The answers to these and other questions must be known before we proceed along the path outlined in S. 548. I support the goal of the legislation, and I have worked with Senator Metzenbaum last November and again earlier this month to insure that retire benefits were not cut off. One of the objectives of extending the protection period has been to allow this committee sufficient time to develop a satisfactory permanent solution.

We have a distinguished group of witnesses today. I welcome all of you, and I look forward to receiving your testimony.

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## PREPARED STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM THE STATE OF IOWA

I want to thank Chairman Heflin for scheduling this second morning of hearings on S. 548.

I am as aware as any member of this subcommittee of the ability—and sometimes the need—of the Bankruptcy Code to address social injustices. Last Congress, we enacted a new chapter—chapter 12—designed to allow family farmers a fighting chance to reorganize the only life they've ever known.

We did it because the current economic condition of American agriculture demanded it.

We did it because the existing code didn't work for a defined group of Americans.

In short, we did it because it was equitable to do so—even though some bankruptcy law "purists" spoke against it.

The proposal we address today stands for the proposition that it's inequitable for a company to use the benefits of the code to reorganize on the backs of its former employees.

While I find it difficult to quarrel with this proposition, I look forward to today's testimony to determine whether this particular remedy is the best way to achieve the goals we all want to achieve. Thank you, Mr. Chairman.

Senator **HEFLIN**. Our first witness today is Mr. Staughton Lynd, of the Legal Defense Association, representing Solidarity.

Mr. Lynd, we appreciate your presence here and we look forward to you testifying but not from that stack of papers that you have there.

## STATEMENT OF STAUGHTON LYND, COUNSEL, SOLIDARITY USA, ACCOMPANIED BY ALICE LYND, COCOUNSEL

Mr. **LYND**. Mr. Chairman and members of the Senate Judiciary Committee, my name is Staughton Lynd. I represent Solidarity USA, the Youngstown-based organization of LTV retirees. The proposals we make have been endorsed by retiree organizations in Aliquippa, PA, East Chicago, IN, Pittsburgh, PA, and also by the Johnstown Senior Unemployed Steel Worker Committee of Johnstown, PA, hourly employees of Bethlehem Steel who fear that their turn in bankruptcy may be next.

It is our belief that the Metzenbaum-Stokes bill in its present form is a good bill but needs to be strengthened, we are also joined by Retirees Against Greed and Exploitation (R.A.G.E.) of Canton, OH, four of whose members are here today. We think that in making our proposals we speak for more LTV retirees than any other person or organization.

Mr. Chairman, attached to my testimony as an appendix are the four amendments to the Metzenbaum-Stokes bill in its present form that Solidarity USA and its associate organizations present for your consideration. In these brief remarks, I wish to address only the first and most important of the four proposed amendments, namely, that any provision for modification of retiree benefits in bankruptcy should become effective only after nonbankruptcy legislation is in place to guarantee benefits in full.

The Metzenbaum-Stokes bill in its present form permits retiree benefits to be modified. In its present form, the bill permits modification either by negotiation between the bankrupt company and the union representing hourly employees or by the bankruptcy judge.

Although the Metzenbaum-Stokes bill is entitled the Retiree Benefits Security Act of 1987, it does not give retirees security with respect to their benefits. On the contrary, it leaves retirees subject to continuing gnawing uncertainty as to whether their benefits may be modified at some future date.

Mr. Chairman, as a token of the concern felt on this matter by the retirees whom I represent, let me present to you for inclusion in the record these petitions signed by 8,733 persons, signed within the last 2 weeks in only the three communities of Youngstown, OH, Warren, OH, and New Castle, PA.

The petition says:

> We, the undersigned, hereby petition our Representatives and Senators to amend the Metzenbaum-Stokes bill to guarantee the payment in full of retiree health and life insurance benefits.

Now, why do we feel, as LTV retirees, that there is no rational basis for modification of benefits? Mr. Chairman, the LTV Corp. has demonstrated in many ways that its post-petition profitability permits the payment of retiree benefits in full. This is a corporation that told the Pension Benefit Guaranty Corp. that it could not make an annual payment of less than $300 million into its pension funds while simultaneously announcing a proposal to invest $500 million in steel facilities alone during the next 2 years.

This is a corporation that paid its 15 top executives $4 million last year, while telling retirees that it could not pay them $400 a month in pension supplements for early retirement. We think that the evidence is overwhelming that LTV Steel should be required to pay retiree benefits in full and we appeal to you not to give a bankruptcy judge ruling in a court hand-picked by LTV and far from the retirees whose lives are affected by its decisions, discretion to modify those benefits.

On the other hand, Mr. Chairman, we recognize that the Metzenbaum-Stokes bill is a general bill, applying not only to LTV Steel but to all companies that in the future may seek relief under chapter 11.

The proponents of the bill in its present form say that if such bankrupt companies are categorically required to pay retiree benefits in full under all circumstances, they may be forced into liquidation. How then can these competing concerns be reconciled?

To Solidarity it seems obvious that the way to protect retiree benefits which deserve to be paid in full, while at the same time to permit bankruptcy courts the flexibility they need in specific situations, is to insure that the provisions of Metzenbaum-Stokes, which permit the modification of retiree benefits, do not become effective until nonbankruptcy legislation is in place which guarantees in full any benefits that may be modified by a bankruptcy court.

Our proposed amendment says exactly that. In the case of the hypothetical company that might be forced into liquidation by a requirement to pay benefits in full, its benefits could be modified but only after legislation is in place to guarantee any amounts by which the benefits are reduced.

Mr. Chairman, there have been at least two deaths in Youngstown because of the LTV bankruptcy. Roy St. Clair, when his heart pains came last July, did not go to the hospital because he did not know how his medical benefits would be paid. This past February, Louis Lipka took his own life because of worry as to whether his medical insurance might again be cut off.

Please do not pass a bill permitting modification of benefits without legislation in place to guarantee benefits in full.

Thank you for your consideration.

[The prepared statement of Mr. Lynd follows:]

## STATEMENT OF SOLIDARITY USA, BY ITS COUNSEL STAUGHTON LYND, ON PROPOSED S. 548 (THE METZENBAUM-STOKES BILL)

Mr. Chairman and Members of the Senate Judiciary Committee:

My name is Staughton Lynd. Together with my wife, I am counsel for Solidarity USA, the Youngstown-based organization of LTV retirees. The proposals I am about to make have been endorsed by Solidarity USA, and also by retiree organizations in Aliquippa, Pennsylvania; East Chicago, Indiana; Pittsburgh, Pennsylvania; and Johnstown, Pennsylvania. We believe that in making these proposals, we speak for more LTV retirees than any other person or organization.

Mr. Chairman, attached to my testimony as an appendix are the four amendments to the Metzenbaum-Stokes bill in its present form that Solidarity USA and its associated organizations present for your consideration. The text of each amendment is preceded by a brief rationale.

Mr. Chairman, in these brief remarks I wish to address only the first of the four proposed amendments. It is the amendment that we consider indispensable, and in the absence of which we could not support the Metzenbaum-Stokes bill.

The Metzenbaum-Stokes bill permits retiree benefits to be modified. In its present form the bill permits benefits to be modified either by negotiation between the bankrupt company and the union representing hourly employees, or by the bankruptcy judge. Although the Metzenbaum-Stokes bill is entitled the "Retiree Benefits Security Act of 1987," it does not give retirees security with respect to their benefits. On the contrary, it leaves retirees subject to continuing gnawing uncertainty as to whether their benefits may be modified at some future date.

There is no rational basis for permitting the retiree benefits promised by LTV to be modified. The LTV corporation has demonstrated its post-petition profitability in a variety of ways. This corporation took away medical benefits from the elderly, but paid its six top executives a total of $4 mil. in 1986. Raymond Hay, Chairman of the Board and Chief Executive Officer, received a salary of $530,000 and a performance bonus of $130,000. This corporation announced in December 1986 that it would invest $500 million in its steel facilities during the next two years, while telling the Pension Benefit Guaranty Corporation that it could not make its annual payment of roughly half that amount into its pension funds. The stock of this corporation increased in value during the first quarter of 1987 by a percentage greater than the percentage increase in the stock of any other American corporation. (New York Times, April 2, 1987) Yet this corporation says it cannot pay its early retirees the $400 a month that it promised to pay them, and sends them a $750 "hardship" payment for three months. The cost of retiree health and life insurance benefits to LTV was only $72 million in 1984, $101 million in 1985, and $99 million in 1986. (LTV 1986 Annual Report, p. 27) But LTV and its creditor banks claim that the company cannot successfully reorganize if it is required to pay these promised benefits in full.

We respectfully submit to you that the evidence is overwhelming. LTV can pay promised retiree benefits in full and reorganize successfully at the same time. Please do not give a bankruptcy judge, ruling in a court hand-picked by LTV and far from the retirees whose lives are affected by its decisions, discretion to modify these benefits.

Proponents of the Metzenbaum-Stokes bill in its present form say that their concern is to prevent bankrupt companies from being forced into liquidation. They argue that if the bill is amended to require full payment of medical benefits by every bankrupt company under all possible circumstances, some companies that might otherwise be able to reorganize might be forced into liquidation. They concede that this reasoning does not apply to LTV, but they emphasize that the Metzenbaum-Stokes bill is a general bill applying to all companies that in the future may seek relief under Chapter 11.

At the same time, President Lynn Williams of the United Steelworkers of America recognized in his testimony on the Metzenbaum-Stokes bill on April 1, that "Congress must make it the public policy of this country that retiree benefits -- once promised and earned from a lifetime of labor -- be paid, in paid in full" (Testimony, p. 11). He further recognized that the proposed Metzenbaum-Stokes bill would leave retiree benefits "unfunded and unguaranteed" and that the "full protection of retiree insurance necessarily demands non-bankruptcy legislation as well" (Testimony, p. 12).

To Solidarity, it seems obvious that the only way to protect the

LTV retiree benefits which deserve to be paid in full, and to accomplish the general goals so well expressed by President Williams, is to ensure that the provisions of Metzenbaum-Stokes which permit the modification of retiree benefits do not become effective until non-bankruptcy legislation is in place which guarantees in full any benefits that may be modified by a bankruptcy court.

Our proposed amendment says exactly that. The amendment would permit any modification of benefits pursuant to the modification provisions of the Metzenbaum-Stokes bill to become effective only after Congress enacts non-bankruptcy legislation that guarantees retiree health benefits in full in the event that such benefits are modified by a bankruptcy court.

Thus, in the case of the hypothetical company that might be forced into liquidation by a requirement to pay benefits in full, its benefits could be modified but only after legislation is in place to guarantee any amounts by which the benefits are reduced.

The question may be raised, where would Congress find the money to guarantee benefits? Consider that, to use the example most often mentioned in our retiree meetings, the $100 million a year required to pay the medical benefits of LTV retirees could be found by diverting to this purpose funds presently given to the Nicaraguan contras. A general fund to guarantee all retiree medical benefits, of all companies that in the future declare bankruptcy, might be created by a tax on imported steel.

Mr. Chairman, there have been at least two deaths in Youngstown because of the LTV bankruptcy. Roy St. Clair, when his heart pains came last July, did not go to the hospital because he did not know how his medical bills would be paid. This past February Louis Lipka took his own life because of worry as to whether his medical insurance might again be cut off.

Please do not pass a bill permitting modification of benefits without legislation in place to guarantee benefits. Thank you.

## APPENDIX

Amendment 1 (delaying the effective date of those provisions of the bill permitting modification of benefits until non-bankruptcy legislation is in place that guarantees retiree medical benefits).

This amendment expresses the most serious objection of LTV retirees to the Metzenbaum-Stokes bill in its present form. Unless the language of the bill concerning modification of benefits is strengthened before final passage in both houses of Congress, Solidarity USA, the thousands of retirees for whom Solidarity speaks, and associated organizations, would find it impossible to support the legislation.

Consider that LTV retirees are presently receiving their medical and life insurance benefits in full. The Metzenbaum-Stokes bill, in contrast, permits modification of benefits either by the bankruptcy judge or by the union and bankrupt company through negotiations. The Metzenbaum-Stokes bill, although entitled the "Retiree Benefits Security Act of 1987," does not give retirees security with respect to their benefits. On the contrary, it leaves them uncertain as to whether their benefits may be modified at some future date.

Proponents of the Metzenbaum-Stokes bill in its present form say that their concern is to prevent bankrupt companies from being forced into liquidation. They argue that if the bill is amended along the lines of H.R. 1488 (introduced in the House by Congressman Traficant) to require full payment of medical benefits by every bankrupt company under all possible circumstances, some companies that might otherwise be able to reorganize would be forced into liquidation. They concede that this reasoning does not apply to LTV, which has demonstrated its post-petition profitability in a variety of ways, but they emphasize that the Metzenbaum-Stokes bill is a general bill applying to all companies that in the future may seek relief under Chapter 11.

At the same time, President Lynn Williams of the United Steelworkers of America recognized in his testimony on the Metzenbaum-Stokes bill on April 1, that "Congress must make it the public policy of this country that retiree benefits -- once promised and earned from a lifetime of labor -- be paid, be paid in full" (Testimony, p. 11). He further recognized that the proposed Metzenbaum-Stokes bill would leave retiree benefits "unfunded and unguaranteed" and that the "full protection of retiree insurance necessarily demands non-bankruptcy legislation as well" (Testimony, p. 12).

To Solidarity, it seems obvious that the only way to accomplish the goals so well expressed by President Williams is to ensure that the provisions of Metzenbaum-Stokes which permit the modification of benefits do not become effective until non-bankruptcy legislation is in place which guarantees in full any benefits that may be modified by a bankruptcy court.

Amendment 3 says exactly that. The amendment would permit any modification of benefits pursuant to the modification provisions of the Metzenbaum-Stokes bill to become effective only after Congress enacts non-bankruptcy legislation that guarantees retiree health benefits in full in the event that such benefits are modified by a bankruptcy court.

AMENDMENT 1 to S. 548 (delaying the effective date of those provisions of the bill permitting modification of benefits until non-bankruptcy legislation is in place that guarantees retiree medical benefits)

Add to proposed Section 1114 the following subsection (j):

"(j) This Act and the amendments made by this Act shall become effective on the date of enactment of this Act and shall be effective with respect to cases commenced under chapter 11 of title 11, United States Code, in which a plan for reorganization has not been confirmed by the court as of October 2, 1986, and in which any retiree benefit, as defined in section 1114 of title 11, United States Code, is still being paid on October 2, 1986 or thereafter, and in cases that become subject to chapter 11, title 11, United States Code, after October 2, 1986, except that no modification of retiree benefits as provided for in this Act and the amendments made by this Act shall become effective unless and until the Congress of the United States enacts legislation that guarantees retiree health benefits in full in the event that such benefits are modified by a bankruptcy court, which legislation shall include language expressly declaring an intent to make effective the provisions of this Act and the amendments made by this Act that permit the modification of retiree benefits."

Amendment 2 (providing that where a union has a conflict of interest in representing both active and retired workers in bankruptcy negotiations, a representative for the class of retirees should be appointed by the bankruptcy judge as set forth in In re Century Brass Products, Inc., 122 LRRM 2833, 2841 (2d Cir. 1986))

S 548 as presently drafted states in Section 1113(h) and (i) that:

> "(h) The labor organization which is the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section is, for purposes of this section, the authorized representative of those persons receiving any retirement benefits covered by such agreement, unless such labor organization elects not to serve as the authorized representative of such persons.
>
> (i) In cases where the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section elects not to serve as the authorized representative of those persons receiving any retirement benefits covered by such an agreement, the court, upon motion of such persons, and after notice and hearing, shall appoint a committee of retired employees, from among such persons, to serve as the authorized representative of such persons, under this section."

This language means that LTV retirees must be represented by the United Steelworkers of America in the bankruptcy court, no matter what the retirees may desire or how the union may conduct itself, so long as the union wants to provide the representation.

This language should be self-evidently unacceptable. LTV retirees are no longer members of the United Steelworkers of America. They do not pay dues. There is no mechanism such as a monthly local union meeting whereby the union is required to account to retirees, and, above all, no requirement that any arrangements negotiated by the union on behalf of retirees must be submitted to the retirees for approval.

Moreover, the proposed language of Section 1113(h) and (i) is a step backward from existing law. The decision of the Second Circuit Court of Appeals in In re Century Brass, Inc., 122 LRRM 2833, 2841 (2d Cir. 1986), provides that the union which represented retirees when they were active employees will "presumptively" represent retirees in bankruptcy court, but if it should appear to the judge that the union has a conflict of interest in attempting to represent active and retired employees at the same time, he can appoint a separate representative for the retirees. This decision is presently the law of the LTV bankruptcy proceeding, since the bankruptcy court is located in the Second Circuit.

Amendment 2 seeks to give hourly retirees the same opportunity to select their own bankruptcy representative that proposed Section 1114 gives to salaried retirees.

AMENDMENT 2 to S. 548 (providing that where a union has a conflict of interest in representing both active and retired workers in bankruptcy negotiations, a representative for the class of retirees should be appointed by the bankruptcy judge as set forth in In re Century Brass Products, Inc., 122 LRRM 2833, 2841 (2d Cir. 1986))

Add to Section 1113 the following subsection (j):

"(j) The court, upon motion of recipients of retiree benefits covered by a collective bargaining agreement covered by section 1113 of this title, or upon its own initiative, shall, after motion and hearing, and if it finds that the labor organization indicated by subsection (h) of this section has an actual conflict of interest in representing both its active and retired workers, appoint a committee of retired employees from among such persons to serve as the authorized representative of such persons under this title."

Amendment 3 (ensuring that claims for retiree medical benefits that came due before filing of a bankruptcy petition continue to be paid promptly and in full as well as claims that come due during the post-petition Chapter 11 period).

S. 548 (the Senate version of the Metzenbaum-Stokes bill) as presently drafted states in proposed Section 1114(d)(1):

> "(d)(1) Notwithstanding any other provision of this title, the debtor in possession, or the trustee if one has been appointed under the provisions of this chapter (hereinafter in this section 'trustee' shall include a debtor in possession), shall pay and shall not modify any retiree benefits to or for the benefit of retired employees and their spouses and dependents, except that [here follows the language permitting modification of benefits which is addressed in proposed Amendment 3]"

Proposed Section 1114(d)(2) states that any payment required to be made by this section after the filing of the bankruptcy petition and before a reorganization plan has been approved and become effective has the status of an "administrative [highest priority] expense."

Proposed Section 1114(d)(1) and (d)(2) appear to cover only medical benefits that come due after the bankruptcy petition is filed. Thus Attorney Nathan Feinstein, testifying about the Metzenbaum-Stokes bill on behalf of the American Bar Association on April 1, stated:

> "Senate Bill 548 . . . elevates medical and disability retiree claims which arise out of pre-petition contracts to 'cost of administration' (first priority) status, but only those which come due during the post-petition Chapter 11 period." (Testimony, p. 8)

Where does this leave a medical benefit that "came due" before the bankruptcy petition was filed but had not been paid as of the date of filing? or a hospitalization that began before the bankruptcy filing but still continued as of that date? Solidarity has encountered situations where:

1. A medical expense was incurred and submitted for payment of insurance benefits before the petition was filed, but the insurance company had not determined the amount payable or had not paid the amount as of the date the petition was filed;

2. A person entered a hospital with pre-certification of benefits, and the petition was filed during the hospitalization, so that some expenses were incurred pre-petition and other expenses were incurred post-petition, and all were billed post-petition although authorized pre-petition.

Amendment 1 seeks to ensure continuation of insurance coverage without any gaps and to avoid litigation in such "fence-straddling" situations.

AMENDMENT 3 to S. 548 (ensuring that claims for retiree medical benefits that came due before filing of a bankruptcy petition continue to be paid promptly and in full as well as claims that come due during the post-petition Chapter 11 period)

Add to proposed Section 1114(d)(1) the following words:

"(d)(1) Notwithstanding any other provision of this title, the debtor in possession, or the trustee if one has been appointed under provisions of this chapter (hereinafter in this section 'trustee' shall include a debtor in possession), shall pay promptly and in full and shall not modify any retiree benefits to or for the benefit of retired employees and their spouses and dependents, including retiree medical benefits arising from pre-petition contracts that came due before filing of a bankruptcy petition, except that . . . ."

Amendment 4 (explaining that the words "necessary to permit the reorganization of the debtor" in Section 1113(b)(1)(A) and in proposed Section 1114(e)(1) and (f)(1) mean "necessary to prevent the debtor's liquidation" as set forth in *Wheeling-Pittsburgh Steel v. United Steelworkers*, 791 F.2d 1074, 1089 (3d Cir. 1986))

This amendment is prompted by some observations of Attorney Paul Whitehead of the United Steelworkers of America at a meeting with representatives of Solidarity USA and other retiree groups on March 27. Mr. Whitehead indicated that it would be much more difficult for a bankrupt company to persuade a court to permit the modification of retiree benefits if the court adopted an interpretation of the words "necessary to permit the reorganization of the debtor" suggested by the Third Circuit Court of Appeals in the Wheeling-Pittsburgh bankruptcy.

The words "necessary to permit the reorganization of the debtor" were before the Third Circuit as part of then-existing Section 1113 of the bankruptcy code. In order to modify a collective bargaining agreement of a bankrupt company, according to Section 1113, it must be shown that the modifications proposed are "necessary to permit the reorganization of the debtor."

Wheeling-Pittsburgh tried to argue that "necessary to permit the reorganization of the debtor" allowed the court to look at a bankrupt company's long-run prospects for profitability, and to permit modification of benefits that seemed likely to enhance that profitability. The court rejected this approach and said that, to obtain modifications, the company must show that the modifications are "necessary to prevent the debtor's liquidation" in the short run.

This issue is highly relevant to LTV, which is clearly able to pay retiree benefits in full in the short run, but the long-run prospects of which are inevitably less certain.

The meaning of "necessary to permit the reorganization of the debtor" arises again in connection with the Metzenbaum-Stokes bill, because proposed Section 1114 makes this test the principal test in determining whether a bankrupt company should be permitted to modify retiree benefits. Attorney Whitehead said that it is critical to make the Third Circuit's interpretation of these words a part of the legislative history of Metzenbaum-Stokes, so that courts would follow it in applying Metzenbaum-Stokes, if enacted.

Solidarity thinks it would be simpler and more sure to make the desired interpretation part of the statute, and seeks to do so in Amendment 4.

AMENDMENT 4 to S. 548 (explaining that the words "necessary to permit the reorganization of the debtor" in Section 1113(b)(1)(A) and in proposed Section 1114(e)(1) and (f)(1) mean "necessary to prevent the debtor's liquidation" as set forth in Wheeling-Pittsburgh Steel v. United Steelworkers, 791 F.2d 1074, 1089 (3d Cir. 1986))

Add to Section 1113(b)(1)(a), to proposed Section 1114(e)(1), and to proposed Section 1114(f)(1), in each case immediately following the words, "necessary to permit the reorganization of the debtor," the following words:

"that is, necessary to prevent the debtor's liquidation"

* * *

By Mr. METZENBAUM (for himself, Mr. Heinz, Mr. Glenn, Mr. Specter, Mr. Byrd, Mr. Lugar, Mr. Riegle, Mr. Durenberger, Mr. Simon, Mr. Rockefeller, Mr. Levin, and Mr. Boschwitz):

S. 548. A bill to amend title 11, United States Code, the Bankruptcy Code, regarding benefits of certain retired employees; to the Committee on the Judiciary.

### RETIREE BENEFITS SECURITY ACT

● Mr. METZENBAUM. Mr. President, today I am introducing the Retiree Benefits Security Act of 1987, a bill to amend the Federal Bankruptcy Code to protect retiree health and life insurance benefits. I am joined in this effort by Senators Heinz, Glenn, Specter, Byrd, Lugar, Riegle, Durenberger, Simon, Levin, Rockefeller, and Boschwitz.

It is hard to imagine anything more frightening for a senior citizen than the threat of losing health and life insurance benefits. Yet it is a sad fact that in too many instances these benefits are not secure.

Our bankruptcy laws totally ignore the needs and rights of retirees. In a bankruptcy retirees become unsecured creditors—told to stand at the end of the line.

Those who build a company deserve better. They deserve to be treated in a fair and compassionate manner. They have earned that right.

No situation dramatizes this fact more than the unilateral suspension of medical insurance by the LTV Corp.

This action affected 78,500 retirees and their families. On July 28 the Senate Judiciary Committee convened an emergency hearing in Cleveland and heard from some of those most effected. Their testimony brought tears to every member's eyes. Never have I heard such a sense of hopelessness and concern.

In order to enable Congress to fully address the issue of retiree health benefits and to protect LTV retirees, I authored an amendment to the continuing resolution mandating the continuation of benefits to union and nonunion retirees through May 15, 1987. The bill I am introducing today is intended to make a permanent change in our bankruptcy laws.

Mr. President, LTV is not the only bankrupt company to attempt suspending retiree health coverage. In fact, after Congress acted last year the A.H. Robins Corp. requested permission from a bankruptcy judge to terminate its health coverage to retirees.

It is a well known fact that Robins is in bankruptcy not because it is unprofitable, but because it is attempting to shield itself from damage suits over its Dalkon shield product. In fact A.H. Robins reported 1986 earnings of nearly $82 million, an increase of nearly 8 percent over its 1985 level. Its action in asking to get out of its promise to provide retiree benefits is a clear abuse of our bankruptcy laws. Fortunately our stopgap measure is protecting these retirees through May 15 of this year.

This is another example of why the legislation I am introducing today is so urgent.

This measure clarifies the current meaning of existing law as it relates to collectively bargained retiree benefits. It affords retirees the same protection as active workers by prohibiting termination or modification of any benefit until the union and the company have negotiated in good faith. And if no agreement is reached, it requires a hearing and a court determination before any changes can be made. This is what Congress intended in enacting the Bankruptcy Reform Amendments of 1984.

This measure also recognizes the very special nature of retiree health and life insurance benefits for all retirees, both union and nonunion. It prevents bankrupt companies from terminating or reducing these benefits unless a bankruptcy judge determines after a hearing that it is necessary to permit reorganization of the company, all parties will be treated fairly, and the equities of the situation clearly favor such change. And it makes sure that retirees continue to be protected as the company reorganizes and comes out of bankruptcy.

Mr. President, if our bankruptcy laws are to have any sense of compassion and justice, any concern for those least able to protect themselves from the power of the Wall Street bankruptcy lawyers, we should enact this legislation quickly. And, Mr. President, I want the retirees of LTV and A.H. Robins to know that if necessary, in order to enable Congress to complete its consideration of this measure, I stand prepared to extend the stopgap measure beyond May 15, 1987.

I urge my colleagues to support this measure. Mr. President, I ask unanimous consent that a copy of the bill be printed in the Record.

There being no objection, the bill was ordered to be printed in the Record, as follows:

### S. 548

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That this Act may be cited as the "Retiree Benefits Security Act of 1987".

Sec. 2. (a) Section 1113(f) of title 11, United States Code, is amended by inserting "(including any provision relating to benefits for retired employees)" after "provisions" the first place it appears.

(b) Section 1113 of title 11, United States Code, is amended by adding at the end thereof the following:

"(g) Claims arising under any collective bargaining agreement covered by this section, or as a result of the rejection of any such agreement, shall not be limited by section 502(b)(7) of this title.

"(h) The labor organization which is the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section is, for purposes of this section, the authorized representative of those persons receiving any retirement benefits covered by such agreement, unless such labor organization elects not to serve as the authorized representative of such persons.

"(i) In cases where the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section elects not to serve as the authorized representative of those persons receiving any retirement benefits covered by such an agreement, the court, upon motion of such persons, and after notice and hearing, shall appoint a committee of retired employees, from among such persons, to serve as the authorized representative of such persons, under this section.".

(c) Subchapter I of chapter 11 of title 11, United States Code, is amended by adding at the end thereof the following new section:

**"§ 1114. Payment of benefits to retired employees**

"(a) For purposes of this section, the term 'retiree benefits' means benefits for retired employees and their spouses and dependents, under any plan, fund, or program maintained or established in whole or in part by the debtor prior to filing a petition commencing a case under this title (through the purchase of insurance or otherwise) for the purpose of providing medical, surgical, or hospital care benefits, or benefits in the event of sickness, accident, disability, or death.

"(b) For purposes of this section, the term 'authorized representative' means the authorized representative designated pursuant to subsection (h) or (i) of section 1113 of this title, or, in the case of recipients of retiree benefits not covered by a collective bargaining agreement covered by section

1113, the authorized representative appointed pursuant to section (c) of this section.

"(g) The court, upon motion of recipients of retiree benefits not covered by a collective bargaining agreement covered by section 1113 of this title, and after notice and a hearing, shall appoint a committee of retired employees from among such persons to serve as the authorized representative of such persons under this section.

"(d)(1) Notwithstanding any other provision of this title, the debtor in possession, or the trustee if one has been appointed under the provisions of this chapter (hereinafter in this section 'trustee' shall include a debtor in possession), shall pay and shall not modify any retiree benefits to or for the benefit or retired employees and their spouses and dependents, except that—

"(A) the court, on motion of the trustee, and after notice and a hearing, may order modification of such payments, pursuant to the provisions of subsections (e), (f), and (g) of this section, or subsection (e) of section 1113 of this title, or

"(B) the trustee and the authorized representative of the recipients of those benefits may agree to modification of such payments,

after which such payments as modified shall continue to be paid by the trustee.

"(2) Any payment required to be made by any provisions of this section after the date of the filing of the petition and before a plan confirmed under section 1129 of this title is effective has the status of an allowed administrative expense as provided in section 503 of this title.

"(e) With respect to retiree benefits that are not covered by a collective bargaining agreement covered by section 1113 of this title, the court, upon motion of the trustee, and after notice and a hearing, shall enter an order providing for modification in the payment of such retiree benefits, only if the court finds that—

"(1) the modifications in the retiree benefits sought by the trustee are necessary to permit the reorganization of the debtor and assure that all creditors, the debtor, and all of the affected parties are treated fairly and equitably; and

"(2) the balance of the equities clearly favors the entry of an order authorizing the trustee to modify the retiree benefits to the level sought by the trustee;

except that in no case shall the court enter an order providing for a modification lower than the level described in paragraphs (1) and (2).

"(f) With respect to retiree benefits that are covered by a collective bargaining agreement covered by section 1113 of this title, and only after such an agreement is rejected under such section, the court, upon motion of the trustee, and after notice and a hearing, shall enter an order providing for such modification in the payment of such retiree benefits as the court finds—

"(1) is necessary to permit the reorganization of the debtor and assures that all creditors, the debtor, and all of the affected parties are treated fairly and equitably; and

"(2) is clearly favored by the balance of the equities,

except that in no case shall the court enter an order providing for such modification which provides for a modification to a level lower than that proposed by the trustee in the proposal found by the court in the section 1113 proceeding to have complied with the requirements of subsections (b) and (c) of section 1113.

"(g)(1) Prior to a court issuing a final order under subsection (e) of this section, if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may authorize the trustee to implement interim changes in retiree benefits not provided to a collective bargaining agreement covered by section 1113 of this title.

"(2) Any hearing under this subsection shall be scheduled in accordance with the needs of the trustee.

"(3) The implementation of such interim changes does not render the motion for modification moot.

"(h) In calculating the amounts of the claims for unpaid future retiree benefits, or for any retiree benefits not provided due to modifications authorized pursuant to this section, and in calculating the amounts payable pursuant to any plan for such claims, any retiree benefits paid between the filing of the petition and the time a plan confirmed under section 1129 of this title becomes effective shall not be deducted or offset from such amounts unless otherwise agreed by the debtor and the authorized representative of the recipients of those retiree benefits.

"(i) No claim for retiree benefits shall be limited by section 502(b)(7) of this title.".

(d) Section 1122 of title 11, United States Code, is amended—

(1) in subsection (a), by striking out "subsection (b)" and inserting in lieu thereof "subsections (b) and (c)"; and

(2) by adding at the end thereof the following:

"(c) A plan shall place all claimants for retiree benefits (as such term is defined in section 1114), in a separate class consisting only of such claimants.".

(e) Section 1129(b)(2) of title 11, United States Code, is amended by—

(1) redesignating subparagraph (C) as subparagraph (D); and

(2) inserting between subparagraph (B) and subparagraph (D), as redesignated herein, the following:

"(C) With respect to a class of claimants for retiree benefits (as such term is defined in section 1114)—

"(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim, property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

"(ii) the plan provides that each holder of a claim of such class receive such value as found by the court to represent the minimum reduction in retiree benefits consistent with the ability of the debtor to provide such retiree benefits after confirmation of the plan.".

(f) The table of sections for subchapter I of chapter 11, title 11, United States Code, is amended by adding at the end thereof the following new item:

"1114. Payment of benefits to retired employees.".

(g) This Act and the amendments made by this Act shall become effective on the date of enactment of this Act and shall be effective with respect to cases commenced under chapter 11 of title 11, United States Code, in which a plan for reorganization has not been confirmed by the court as of October 2, 1986, and in which any retiree benefit, as defined in section 1114 of title 11, United States Code, is still being paid on October 2, 1986 or thereafter, and in cases that become subject to chapter 11, title 11, United States Code, after October 2, 1986.●

* * *

Senator HEFLIN. Thank you, Mr. Lynd.

Would you like to introduce the lady with you?

Mr. LYND. Yes. This is cocounsel for Solidarity USA, my wife, Alice Lynd.

Senator HEFLIN. We are delighted to have you with us.

Mr. Lynd, we appreciate your testimony and we understand your concerns with the legislation as currently drafted, but there are, of course, many people who think that the legislation has already gone too far in changing the existing balance between creditors. The subcommittee certainly will consider your proposals and those proposals of people who say that it has gone too far during our efforts to try to reach a good bill. I think everybody realizes that compromise is going to have to be made, but we appreciate your testimony, your position on the matter and hopefully we will come up with a bill that is fair to all sides.

Mr. LYND. If I might just respond briefly, Mr. Chairman, of course one of the questions raised about nonbankruptcy legislation is where would the money come from to guarantee benefits. I want to be sure that the committee appreciates that according to LTV's most recent annual report, the amount of money spent on medical benefits in each of the last 3 years was only $100 million a year. That is the amount of money currently being appropriated to support the Contras in Nicaragua; it could be easily raised, let us say, by an import tax on steel.

Senator HEFLIN. Senator Metzenbaum?

## OPENING STATEMENT OF HON. HOWARD M. METZENBAUM, A U.S. SENATOR FROM THE STATE OF OHIO

Senator METZENBAUM. Let me say, Mr. Lynd, you and your wife have done a superb job in analyzing the bill and being legal counsel for Solidarity. Solidarity itself is to be commended because I know of no single effort of a similar nature where a group of people organized, brought in counsel, and have done as much to protect the rights of the retirees as have you. You working with the union, which has also certainly been very effective and very concerned and very involved, have been very effective. I think all of us owe you a great debt of appreciation, because I have no idea how you are managing, but I would guess a lot of this is the work of love and you certainly don't have a big corporate client to represent. Your analysis is excellent and you raise some very valid points in your testimony and I am hopeful that we will be able to address them.

As a matter of fact, I think that we do need to improve the langauge regarding representation of retirees to make sure that the process is a fair one for appointing a representative for union and nonunion retirees, and I feel confident that we should be able to work out some language that is right and appropriate in that respect, but I think your point has great validity.

Then we need to clarify the fact that the benefits are to continue without interruption when a company files for chapter 11, regardless of whether the claim arose before or after the filing, and I think that is a very astute observation on your part and I think we can zero in on that issue and probably be able to improve the language.

Now, the bill currently requires the company to prove that a modification in benefits is necessary to permit reorganization. Now, that is the same standard that current law imposes on a company which asks a court to terminate a collective bargaining agreement, and you know that.

The third circuit has held that this language means "necessary to prevent liquidation." That is what I intend S. 548 to require. I agree with you that we need to clarify that in order to seek a modification of the benefits, a company must prove that it is necessary to prevent liquidation.

Now, I am also in complete agreement with your testimony that "the evidence is overwhelming that LTV can pay promised retiree benefits in full and reorganize successfully at the same time." With the clarification you recommend, the court can only modify these benefits when necessary to prevent liquidation. I think it is clear that S. 548 will prevent LTV from unilaterally terminating retiree benefits. In fact, I believe that LTV has made the case for us and I am happy for them that they are making that case, because here is an ad that was from the Plain Dealer in Cleveland—I do not know if you saw it—in which they say it is not going to be easy, and then they go on to say we are confident we can create something of lasting value at LTV, after 9 months of operation as a chapter 11 company we have reached a definite conclusion, we can successfully reorganize the LTV Corp. and create something of lasting value.

Now, that to me is extremely encouraging. I think everybody in this room would like to see LTV make it on its own. I know the chairman would, I would, everybody in the room would, and I think that is the bottom line. I am hopeful that LTV will be able to do exactly that which they said they are capable of doing, and I think you and I would agree, the chairman I think would agree, all would agree that their successful reorganization should not be at the price of the retirees. I think that we are all committed to be helpful in that respect.

I want to thank you for all of the assistance that you have given us as this matter has proceeded along the legislative process.

Mr. LYND. On behalf of the people I represent, Senator, we certainly do thank you for those remarks.

Senator METZENBAUM. Thank you.

Senator HEFLIN. Our next witness, representing the Retired Employees' Benefits Coalition, Inc., REBCO, the retired Bethlehem Steel employees, Mr. Jere Y. Heisler, the president, and then we have as another person on the panel, the Retiree Subcommittee of the Official Unsecured Creditors' Committee of Kaiser Steel, Mr. Carl Eklund, the senior director of the law firm and general counsel for the subcommittee.

Mr. Heisler?

## STATEMENTS OF A PANEL CONSISTING OF JERE Y. HEISLER, PRESIDENT, RETIRED EMPLOYEES' BENEFITS COALITION, INC., ACCOMPANIED BY BRUCE DAVIS, COUNSEL, AND CARL A. EKLUND, COUNSEL, RETIREE SUBCOMMITTEE OF THE OFFICIAL UNSECURED CREDITORS' COMMITTEE OF KAISER STEEL

Mr. HEISLER. Mr. Chairman, may I first introduce our cocounsel, Mr. Bruce Davis, who is going to sit with us.

In the interest of time, as you indicated, I will just comment on our testimony which you have accepted into the record.

I appreciate this opportunity to speak to you today on behalf of our organization of retired salary Bethlehem Steel employees. Our coalition, called REBCO, stands for Retired Employees' Benefits Coalition. There are approximately 20,000 retired Bethlehem Steel salaried employees. We represent clerical people, technical people, mill foremen, mill superintendents, plant managers, salesmen, corporate staff, and management people.

One important point: Not any of these people are represented by a union. You might call us the retired company people. We began organizing REBCO on January 6 of this year. Today, almost 8,000 people of this 20,000 group have contributed to our organization. That, sir, is a pretty fair action group gathered in a very short period of time. And why has this happened?

Mr. Chairman, we are scared to death of what might happen to our pensions, our hospital benefits, our life insurance if Bethlehem Steel elects to file for bankruptcy under chapter 11 as the law exists today.

There have been public assurances from our chairman, Mr. Williams, that "we do not plan for filing bankruptcy at this time." However, Bethlehem has a pension fund which today is underfunded by almost $1.2 billion. They also have to compete in the marketplace with LTV, Wheeling-Pittsburgh, where their costs are now lower compared to Bethlehem by virtue of pension benefits which they have dumped onto the Federal Government.

Will Bethlehem follow a similar pattern? We do not know but we are still very concerned and very scared. Sir, I feel reasonably qualified to speak on behalf of this group by virtue of my family background in steel and 36 years of service with Bethlehem. My dad worked in the Bethlehem plant as a foreman for 42 years. My mom worked as a clerk in the sales department for 21 years. I started with 17 years of service in the steel operations at the Sparrows Point plant, which is outside of Baltimore, and then I worked for 19 years in the corporate offices in production scheduling.

I would like to take this opportunity to express on behalf of our group and their families our total support for S. 548 and its companion bill, H.R. 1186. The recent wave of bankruptcies and reorganizations, especially in the steel industry, is presenting new and unforeseen problems for us retirees.

The use of the Bankruptcy Code by corporations to cut themselves loose from their obligations and commitments to former employees, sir, is a travesty of justice. Our bankruptcy laws should not permit companies to reduce their labor costs by renouncing their contractual moral obligations to their retirees.

Retirees are different. We are individuals, not a corporate entity, contrasted to the position of creditors in a bankruptcy, sir, we have no options. Our planned reliance on retirement benefits for which we worked a lifetime must not be easily and quickly washed away.

In this great nation of ours, founded on the principles of justice, fairness, and the rights of individuals, it is inexcusable that we permit companies to escape into chapter 11 bankruptcy and dump their retirees at bankruptcy's door. Chapter 11 may work for the troubled companies, it does not work for retirees. We need to recognize that retirees have an unusual and an especially vulnerable position in bankruptcy and we need to give the courts the statutory grounds to protect them.

S. 548 and H.R. 1186 are very positive steps toward this goal. On behalf of the 20,000 retired salaried Bethlehem Steel colleagues and millions of other retired people who I believe share our uneasiness, we want to thank you, Mr. Chairman, and this subcommittee for your concern and your efforts on our behalf.

Thank you.

[The prepared statement of Mr. Heisler follows:]

## STATEMENT
## OF
## JERE Y. HEISLER, PRESIDENT
## RETIRED EMPLOYEES' BENEFITS COALITION, INC.
## ("REBCO")

Mr. Chairman:

I appreciate this opportunity to speak today on behalf of our organization of retired SALARIED Bethlehem Steel employees. Our Coalition, REBCO, is officially incorporated as the "Retired Employees' Benefits Coalition, Inc."

There are approximately 20,000 retired Bethlehem Steel SALARIED employees we seek to represent: clerical & technical people, mill foremen, superintendents, plant managers, salesmen, corporate staff and management people. An important point: none of our people are represented by a union. You might call us: "retired company people."

We began organizing REBCO on January 6th of this year. Today, almost 8,000 Bethlehem Steel SALARIED retirees have financially contributed to our organization --- 40% financial participation in less than four months. We have put together a pretty fair action group in a short period of time.

Mr. Chairman, we're "scared to death" of what might happen to our pension, health and life insurance benefits, if Bethlehem Steel were to file for reorganization under Chapter XI as it reads today.

There have been publicly stated assurances by Bethlehem Steel's Chairman, Mr. Walter Williams, that: "We do not have any plans to file bankruptcy at this time."

However, Bethlehem Steel today has a pension fund which is underfunded by approximately 1.2 billion dollars. Bethlehem Steel today has labor costs greater than LTV Steel and Wheeling-Pittsburgh Steel, and several other basic steel producers, because these companies have dumped certain retirement costs on the Federal Government.

Will Bethlehem Steel do likewise? We do not know and this uncertainty scares our retirees.

I feel reasonably qualified to speak on behalf of these

20,000 retired salaried people. I have a family background in steel and 36 years of personal service with Bethlehem. My Father worked for 42 years as a Shipping Foreman in the Bethlehem Plant; my Mother worked for 21 years as a clerk in Bethlehem's Sales Department. My service was 17 years in steel operations at the Sparrows Point Plant near Baltimore and 19 years in Production Scheduling in Bethlehem's Home Office.

Mr. Chairman, I take this opportunity to express, in behalf of our REBCO members, and their families, support for Senate Bill 548, "The Retiree Benefits Security Act of 1987." We also wish to state our support of H. R. 1186, the House version of S. 548.

The recent wave of corporate bankruptcies and reorganizations we have witnessed in this country, especially in the basic steel sector of our economy, is presenting new and unforeseen problems for retirees. Unfortunately, many of these companies view reorganizing as a panacea which will relieve their business difficulties at the expense of their retirees.

We are here today to say that this course of conduct is not an acceptable solution.

The use of the bankruptcy code by corporations to cut themselves loose from their responsibilities and commitments to former employees creates a social policy problem of potentially immense proportions.

Our laws must not permit companies to reduce labor costs by renouncing their contractual, moral and social obligations to their retirees.

Perhaps most devastated by the termination of health benefits are those workers who have opted for early retirement. For years, unions have negotiated for lower retirement ages. As unionized employees gained improved retirement benefits, companies extended similar benefits to nonunionized employees. The logic was obvious. Thirty years or more working in a steel mill is plenty.

The understanding was that those who had put in their time had earned a decent retirement and I stress: earned a decent retirement. Moreover, early retirement served a broader social purpose by opening up jobs for a younger work force. Lately, as many of our Nation's basic steel companies were faced with economic contractions, early retirement became one means for easing the dislocation as mills shut down and plants closed. Older employees were offered incentives to retire.

Today, these retirees can be left in the lurch. For many, their company health insurance is the only coverage they are eligible for, and the cost of individual insurance is generally prohibitive.

However, Mr. Chairman, an even more pressing need is for Congress to act promptly to extend H. R. 5283, passed in October 1986. The temporary protection provided to retirees and their health and life insurance benefits expires in three weeks -- May 15, 1987. We urge Congress to extend this emergency-type legislation until a more permanent law can be enacted.

Let us be very clear on this point: the certainty of company-provided health care is vital to the security and well being of millions of senior citizens. Congress must not allow companies to dump retirees and break commitments under the guise of corporate reorganization.

Retirees depend on their health insurance coverage on a day-to-day basis. They invested their time with their company. They retired with the expectation of receiving promised benefits. Retirees deserve fairer treatment than sudden termination of these benefits.

Arbitrary action by employers to renege on prior promises and contracts made in good faith, especially where it concerns essential benefits, should not be allowed to continue unchecked under an umbrella of bankruptcy proceedings.

Retirees are different. We are individuals, not corporate entities. Contrasted with the position of business creditors in bankruptcy we have no other options; our planned reliance on retirement benefits -- for which we worked a lifetime -- must not be easily or quickly washed away.

Let us consider the realities of a retiree, over the age of 55, who suddenly is told his health and life insurance plans have been cancelled. Many retirees will not be able to find replacement policies. For those lucky enough to find an available insurance policy, too often that policy is unaffordable. This is true not only for those who need supplemental coverage to Medicare, but also for the thousands of early retirees who are not eligible for Medicare.

The fear and harm of lost benefits affects not just LTV retirees, but all retirees -- within and without the steel industry -- who have been promised benefits upon which they have planned their retirement years.

Retiree health benefits are not a luxury; they are central to the well being of retired Americans. Fairness dictates that retirees be treated equitably and in good faith by their former employer and by our laws.

Retirees are not "just like any other unsecured creditor." We are different ... and our bankruptcy laws should recognize these differences.

To make steel, you need money, which is sometimes "borrowed money." You also need raw materials ... electricity ... transportation ... customers ... and a host of other goods and services. But, all of these elements will not make steel ... or any commodity ... without one other essential element: the worker.

Today, the retired worker, an essential element in making the product, stands at the end of the line.

Today, our bankruptcy laws tell the retired worker to go to the back of the line which leads to the cashier's cage and payouts from the cashier's cage are managed by the bankruptcy court.

Our current laws shamefully permit a company to deprive a retiree or a widow of an entire lifetime of retirement protection.

The typical unsecured creditor in a Chapter XI proceeding is a corporation, often a bank, a utility, or a supplier of goods or services. The typical creditor holds claims - not for something so vital as medical care - but for loans, or electrical power furnished, or goods supplied.

Mr. Chairman, the critical point is this: these creditors usually do business with a large number of companies. If one of their customers default, the loss affects only a portion of their revenues --- they "spread the loss." In fact, their selling prices often include a calculation for bad debts.

How does a senior citizen, a retiree, spread his or her losses?

How shall Congress counsel a retiree to price their decades of services, already provided to the company, to allow for his or her employer's bad debts? Congress, in considering this problem, must keep in focus: if a reorganizing company defaults on an obligation, the typical creditor corporation can seek new business to make up for the loss. The typical Chapter XI creditor can increase the price it charges to all other customers and thereby spread the risk of any one customer defaulting in whole or part. And, if the worse happens, and a debt goes completely sour, the usual creditor takes a tax deduction for a bad debt.

But, how about the retiree and his or her spouse? Since they are owed health and life insurance by the company, they are creditors of the company. But, they are decidedly different from the typical unsecured creditor.

The retiree and the retiree's spouse cannot absorb the loss of their medical care or life insurance coverage by making an adjustment of a balance sheet or increasing their selling price to others. They cannot pass their loss on to customers. The company is their source of private health insurance.

The retiree, unlike the typical creditors, looks to the company -- not for the price of a ton of steel or a kilowatt of power -- but for something so basic and life-giving as decent medical care.

Ask yourself: "What other class of creditors of a reorganizing company is in this position? What other class of creditors depends on the company for the very basics of life and health?"

In short, Mr. Chairman, there are millions of Americans, just like our REBCO members, who worked a lifetime to earn a guarantee for continued employer-provided health coverage. Now, these senior citizens live with the fear that employer-promised benefits may be terminated.

Bankruptcy law should not permit an employer unilaterally to eliminate essential benefits without respecting the rights of the group that relies so heavily on these benefits. In amending the bankruptcy laws regarding retiree welfare benefits, S. 548, "The Retiree Benefit Security Act of 1987," restores fairness and justice to the treatment of retirees in the bankruptcy proceeding.

Mr. Chairman, earlier in this Statement, I noted: "Retirees must be looked upon in bankruptcy as being different from the ordinary creditor." Likewise, salaried retirees must be viewed as being different from retirees represented by international and national unions.

When LTV Steel terminated last July health and life insurance programs for hourly, salaried and retired employees, the Steelworkers struck the company's Indiana Harbor Plant. The strike restored retiree benefits. We applaud the Steelworkers for this decisive and effective display of solidarity.

But the union's first obligation, understandably, is to look out for the best interests of its union members. Salaried employees do not have the collective strength of a union. We cannot realistically consider a strike to restore earned retirement benefits.

To whom, then, shall salaried retirees look to protect their earned and promised retirement benefits? We look to Congress. Thus, we shall continue to seek Congressional support for Senate Bill 548, House Bill 1186, and additional legislation which will address the matter of pension benefits.

In conclusion, Mr. Chairman, we believe Senate Bill 548 and House Bill 1186 can and should be strengthened. We respectfully suggest several amendments: First, we believe Section 1114(e) does not provide salaried retirees with the same protections that are afforded bargaining unit retirees under Section 1114(f). Specifically, Section 1114(e) does not require the Trustee to have complied with the requirements of subsections (b) and (c) of existing Section 1113. Compliance with these existing subsections is important, especially for salaried retirees, since it would be the only method by which they could obtain financial information regarding the bankrupt company in order to defend themselves in a hearing envisioned by Section 1114(e). Furthermore, requiring compliance with these subsections would require the Trustee to meet with the Court-appointed committee required by section 1114(c). Therefore, the committee would have to be appointed before the Trustee could institute any proceeding to modify benefits. Obtaining such representation and financial information is imperative if the proposed beneficiaries are to have any meaningful hearing before a proposed modification of retiree benefits occurs.

Second, we believe that Section 1114(g)(2) should be amended to require compliance with subsections (b) and (c) of Section 1113 before any hearing is held. A Trustee would have an enormous advantage if a hearing is scheduled in accordance with his needs, but before any financial information is provided to the retirees.

Third, we also believe that any motion filed by a Trustee to modify retiree benefits under Section 1114 should be subject to mandatory withdrawal to the District Court upon the motion of any interested party. Such a provision would insure that retirees have an independent and fair hearing from a judge who is not intimately involved in, and primarily concerned with, the reorganization of the bankrupt company.

Again, we would reiterate our strong support for S. 548 and H. R. 1186. The suggested amendments set forth above are only to clarify and strengthen the bills so that the bankruptcy laws can recognize the needs and rights of retirees.

On behalf of our 20,000 retired, salaried Bethlehem Steel colleagues, and the millions of other retirees who I believe share our uneasiness, we thank you, Mr. Chairman, and this Subcommittee for its concern.

In this great nation of ours, founded on the principles of justice, fairness, and concern for the rights of individuals, it is inexcusable that we permit companies to escape into Chapter XI, to dump their retirees at the bankruptcy door, and to emerge profitable with no further obligation to them.

LTV Steel, Wheeling-Pittsburgh, A. H. Robins, Manville, and others may not have entered into bankruptcy to cheat their retirees. But, they show the way for others looking for a way out of their retiree commitments.

Chapter XI may work for the troubled companies, and it may work for the major and usually secured creditors ... but it just does not work for the retirees. We need to recognize that retirees have an unusual and especially vulnerable position in bankruptcy; and we need to give the courts the statutory grounds to protect them. Senate Bill 548 and H. R. 1186 are very positive steps towards this goal.

Thank you.

Senator HEFLIN. Thank you.
Mr. Eklund?

## STATEMENT OF CARL A. EKLUND

**Mr. Eklund.** Thank you, Mr. Chairman, Senator Metzenbaum. I am Carl Eklund. I am appearing on behalf of the Retired Employees of Kaiser Steel, a chapter 11 bankruptcy that has been filed in Denver, CO. There are approximately 7,000 retired employees and our group is unique from the two you have just heard from.

The first was a union, hourly; the second salaried. Our group is both salaried and hourly. I think what Senator Metzenbaum spoke of earlier today about representation for the retirees is a critical provision that needs to be strengthened in your bill.

In section 1114(c), the bill discusses a committee of retired employees being appointed, and I think that is a step in the right direction. What happens is that these retirees also need professional assistance, they need professional experienced counsel, accountants and actuaries to properly do battle with the debtors' team, and if they are put on the creditors committee, as has occurred in the *Kaiser* case in Colorado, that professional assistance is then available for the retirees such that it is very important that the retirees' committee be given positions on the creditors committee.

The decisionmaking process under chapter 11 is weighed very heavily at this time on behalf of management. Management decides whether to file a chapter 11, and whether to pay the benefits. I think what your bill does and what we need is for Congress to even the playing field for the retirees and your bill does that. It requires after the filing of the chapter 11 that the benefits continue until a court, an independent body, makes a determination whether it is necessary to do otherwise. That I believe is a proper balancing of equities here.

I point out another problem and a concern we have. There are competing priority claims. The PBGC will come in as a priority creditor and compete with the very people they are attempting to assist—the retirees, and I would request that the subcommittee consider having the administrative expense priority for retiree benefits have priority over any claim by the PBGC and that that administrative expense continue, including into a chapter 7 when it is determined by the court that it was a feasible benefit.

The issue that is always confronting reorganization in a chapter 11 is that there must be compromise, much like the legislative process, and we are aware of that. We have been in this chapter 11 since February 11, and because of the existence of the Metzenbaum amendment we are negotiating daily, we are at the table, we are trying to get a resolution and I think this legislation assists that process. It has to bring back some balance of power for the retirees.

And while our case is significantly different from the LTV, we do not have many resources in the *Kaiser* case. What we have is very few resources. What we have is a company that has been bled through many reasons, part of those leveraged buyouts from the past, where lawsuits have already been filed trying to address those problems.

There is another problem that I would like your subcommittee to address in its bill. The language of the bill must be clear about what is meant by a program "maintained or established" by the debtor prior to filing. That is critical because in the *Kaiser* case the benefits were terminated just prior to the filing of the chapter 11, and there is certainly an argument for the debtor that since they were terminated prior to the filing that those payments do not need to be made.

I would suggest something along the lines that if any benefits are terminated within 90 days of filing of the bankruptcy, that those payments must also be maintained, because if the retirees see that benefits are being terminated they can then take whatever action they may deem necessary in order to insure their rights and protect their interests in those payments.

Generally, I think your bill takes a very important step in evening the decisionmaking process, and I commend its passage. Thank you.

[Submissions of Mr. Eklund follows:]

# PREPARED STATEMENT OF CARL A. EKLUND

Good morning. If it please the subcommittee, my name is Carl A. Eklund and I am with the firm of Roath & Brega, P.C. in Denver, Colorado. My firm and I have been retained to represent the Retiree Subcommittee of the Official Unsecured Creditor's Committee in the bankruptcy proceedings of Kaiser Steel Corporation which were filed on February 11, 1987 in the United States Bankruptcy Court in Denver, Colorado. The Retiree Subcommittee is comprised of five Kaiser Steel retirees who also sit on the Official Unsecured Creditor's Committee. Two of the members, Ronald Bitonti and Thomas Rabone are hourly retirees of Kaiser Steel; two of the members, Travis Case and Scotty Stevenson, are salaried retirees, and the fifth member, Robert N. Pritchett, is an hourly retiree who serves in an _ex officio_ capacity. Collectively, the Retiree Subcommittee represents the interests of approximately 7,000 hourly and salaried retirees of Kaiser Steel who have had their pension benefits reduced and their medical and long-term disability benefits stopped since the filing of the bankruptcy petition. On behalf of my clients and myself, I would like to express our deep appreciation for the opportunity to address this subcommittee on their behalf.

In the last decade, the bankruptcy laws of this country have been put to uses which could never have been foreseen. The social or business stigma which traditionally accompanied a bankruptcy has now been so eroded that it no longer plays a major factor in the decisionmaking process. Bankruptcy was once viewed as the last resort of the truly desperate -- it is now considered a difficult but viable option whenever a set of circumstances troubling a company or an individual reaches a certain threshold. More importantly, that threshold that is, the level of stress required to file, is much, much lower than it used to be.

I do not mean to imply that this is necessarily a development to be lamented. The bankruptcy law has been used in creative and ingenious ways to solve a host of different problems, often quite successfully. Creative use of the bankruptcy laws as an instrument of financial reorganization, with the resultant benefit when the reorganization succeeds, should, in my view, be encouraged by Congress and the courts. But this encouragement should be tempered by ensuring, as much as possible, that the Bankruptcy Code operates to protect the rights of parties who may suffer severe dislocation by a bankruptcy filing, particularly where those parties do not have the ability to protect or provide for themselves. The retired employees of American business and industry are such a group. We believe S.548 is by and large, a necessary and appropriate response to the problem.

Retirees are basically involuntary creditors. By that I mean that they are not in a position to greatly influence the course a company chooses to take after they have retired. Their benefits are fixed, and they naturally have become dependent upon them. They cannot demand better terms or collateral, or threaten to withhold future goods or services. Because of their fixed income and advanced age, it is tremendously difficult for them to make other arrangements to provide for themselves if their benefits suddenly terminate. In the month of March of 1987 alone, ten retirees of Kaiser Steel died without the benefit of any life insurance payment to their dependents. We believe that Congress should make it as difficult as possible for a company to use the bankruptcy law to modify retiree benefits, consistent with the overall purpose of the Code to promote reorganization wherever possible. We think S.548 strikes the proper balance.

In order to understand the impact and importance of the proposed legislation, I think it would be useful to provide you with a brief overview of the Kaiser Steel situation. We are all familiar with the decline of the steel industry in the United States. Kaiser is certainly a victim of this decline. However, in 1982, Fortune Magazine reported that Kaiser Steel, with 7.3 million shares of common stock outstanding, was sitting on 1.5 billion tons of coal reserves and over $400 million in cash. This type of cash attracts investors, regardless of the rest of the balance sheet, and people such as Ivan Boesky and Irwin Jacobs began to buy up large blocks of Kaiser stock through their investment groups. Kaiser went through 10 chief executive officers in the space of 8 years. These executives, including Edgar Kaiser, Jr., appear to have been chiefly interested in selling the company. In the early 1980's, Kaiser was courted by many people -- some walked away, some made offers which were rejected, and one, Joseph Frates of Oklahoma City, Oklahoma, made an offer of $374.4 million which was accepted. This transaction took the form of what has come to be commonly known as a "leveraged buyout." Kaiser's cash and assets were used to finance the purchase of its own stock on Frates' behalf and Kaiser became a privately-held company. A year later, Frates himself was bought out by his partner, Monte Rial, Colorado Springs, Colorado. Mr. Frates received $41 million in Kaiser assets and cash for Kaiser stock. Thereafter, Mr. Rial paid himself, according to the company's proxy statements and 10-K reports, approximately $2,300,000 a year in salary, not including other compensation and perks. By this time, the steel mill was shut down, and only a small residual amount of steel fabrication operations were taking place. While the company had immense coal reserves, it had only one truly valuable contract for the sale of its coal. The company basically survived until its February 11, 1987 bankruptcy filing by frantically selling assets to pay its bills.

During all this time, Kaiser knew, or certainly should have known, that it owed its retirees an amount variously estimated to be in excess of $800 million. It also certainly knew, as each year went by, the suffering which would result to those 7,000 retirees if their medical benefits and life insurance were suddenly eliminated. If the company had simply been liquidated in 1980, it probably could have provided for its retiree benefits and paid a modest dividend to shareholders. Instead, arbitrators, stock speculators, takeover specialists and shareholders have made immense sums of money at the expense of Kaiser's only real creditors: its retirees.

Kaiser has now filed for bankruptcy protection, having run out of assets to sell to continue funding its retiree benefits on a month-to-month basis. The company is now being run by its preferred shareholders. The preferred shares were originally issued to the common shareholders in 1984 when Mr. Frates purchased the company with its own money. The gained control when preferred dividends went into default in 1986.

Yesterday, at an all day meeting at the Radisson Hotel in Denver, the company presented an outline of its reorganization proposal to its creditors. The company intends to sell its coal properties and all remaining assets except for the old Fontana, California steel mill site, which it intends to develop into a high tech industrial park and toxic waste disposal facility. Previous discussions with counsel for the company have given us the impression that the company would very much like to discharge its obligation to its retirees by "cashing them out" for about 5% of what they are owed. While the details of this proposal may change, and will of course have to await the filing of a plan of reorganization in the bankruptcy court, the consummation of any such proposal is years away.

In the meantime, Kaiser has ceased paying retiree health benefits entirely. Kaiser's pension plans are dramatically underfunded, and either have or will be taken over and administered by the PBGC. The PBGC may have a claim as high as $200 million in the bankruptcy, which, unless changed by S.548, could be granted a greater priority than the claims of the retirees themselves. No medical benefits, life insurance benefits, or long-term disability benefits of any kind are being paid by Kaiser at this time. Kaiser insists it simply does not have the money to make any such payments and continue its operations. The threat of a Chapter 7 proceeding, and the drastic decrease in the assets which remain in Kaiser, prevents the retirees from enforcing what is referred to as the "Metzenbaum Amendment" -- Section 608 of P.L. 99-591, which is the stop gap measure that S.548 would replace. That statute simply mandates that the benefits be continued. The problem with this statute is its apparent inflexibility: it does not allow the court to tailor its relief to the facts of each case. S.548 represents a compromise which, while making it extremely difficult for a company to discontinue retiree benefits, allows the Bankruptcy Court to determine how those benefits should be paid during the pendency of Chapter 11 proceedings, and protects the retirees by giving them priority over other creditors in the event that their benefits are not paid.

This priority is essential, because without it the retirees are simply unsecured creditors like all other unsecured creditors, such as banks, suppliers and other businesses, who have generally dealt with the debtor voluntarily in arms length transactions and are in a position to structure their business relationship in a way to protect their interests.

In the case of Kaiser Steel, there is probably less than $100 million in non-retiree debt, and 80% or more of this is secured by Kaiser's assets. These security interests were taken by these creditors long after Kaiser's 7,000 retirees became involuntary creditors of Kaiser Steel. Unless we are successful in convincing the Bankruptcy Court to set aside many of these liens, these creditors will also be paid at the expense of Kaiser's retirees.

S.548 adjusts the unfairness in these situations by giving the retirees, as involuntary creditors, the legal power to have an effective impact on any reorganization proceedings separate and apart from voluntary creditors of Kaiser who have come into the picture in the meantime. The test for modification of retiree benefits puts the burden where it ought to be: squarely on the debtor. That burden is a difficult one, as shown by the court decisions which have interpreted the identical burden for the rejection of collective bargaining agreements set forth in Section 1113. If the company can meet that burden, however, S548 gives the Bankruptcy Court the flexibility to fashion an interim solution which takes into account all parties' best interests. One of the key benefits of S.548 is that retiree claims will not be reduced to and diluted by parity with general creditors, nor will they even arguably be subject to a one year limitation under Section 502(B)(7) of the Code.

We also support S.548's elevation of unpaid post-petition retiree benefits to the status of administrative claims, where the company has not obtained a court order allowing such a modification. This gives the retiree creditors substantial leverage in a reorganization, and forces the company to negotiate and adopt an acceptable interim solution, so that the retirees are not left totally without coverage as is the case in Kaiser Steel. Failure to provide for such a solution will make it virtually impossible for a company with a sizable group of retirees to confirm a Chapter 11 plan of reorganization over the objection of the retirees. We feel, however, that this section stops somewhat short, and that language should be added affording retirees a priority under Section 507 of the Code, for all unpaid post-petition benefits. This priority should come ahead of any claims by the PBGC. It would be anomalous for the PBGC to be reimbursed for pension guarantees ahead of medical benefits for retirees.

We also support the provision in S.548 that provides for a separate classification for retirees in the plan confirmation process. It is inappropriate to group retirees with general unsecured creditors, for the reasons I have previously stated. Retirees are not at all situated the same as general unsecured creditors, and the resultant dilution of both groups is unfair in terms of voting and cram down. Placing the retirees in a separate class, subject to a separate cram down standard, recognizes that retirees should not be treated as general unsecured business creditors of a Chapter 11 debtor.

The Retiree Subcommittee has authorized me to wholeheartedly endorse S.548. We believe in many areas that the solution to problems such as those faced by the retirees in Kaiser Steel will be legislative rather than judicial. Without this legislation, Kaiser and other Chapter 11 debtors will have much greater powers, under the protections of the Bankruptcy Code to put assets to uses other than the payment of retiree benefits.

In closing, the Retiree Subcommittee would like me to make you aware of certain areas in which they feel Congress could and should go farther in its efforts to protect the retirees of American business, along the following lines:

1. Congress should consider criminalizing conduct such as that which occurred in the Kaiser Steel case whereby the company's assets are exploited for the benefit of arbitrators, stock speculators, takeover specialists and shareholders through leveraged buyouts, when the company knows, or reasonably should know, that the assets which remain will

be dramatically insufficient to provide for its then existing financial commitments to its retirees;

2. Companies should be required to fund retiree health benefits in advance, through a statute similar to ERISA, to guarantee that benefits will be available to retirees even if the company is liquidated; and

3. All unpaid retiree benefits should be granted priority status under § 507 of the Code, superior to the PBGC; and

4. The priority and administrative claim provisions of S.548 should be extended to Chapter 7 cases or any Chapter 11 which is later converted to a Chapter 7.

On behalf of the retiree subcommittee, we hope that you will seriously consider the foregoing, and will move to enact S.548 as expeditiously as possible.

Thank you very much.

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May 12, 1987

The Honorable Howell Heflin
Chairman
Subcommittee on Courts &
  Administrative Practice
United States Senate
Committee on the Judiciary
Washington, D.C. 20510

Re: S-548 -- Questions for Carl A. Eklund

Dear Senator Heflin:

Thank you for your correspondence of May 1, 1987. I apologize for the delay in responding, but I have been away briefly on another matter. On behalf of the Retiree Subcommittee in the Kaiser Steel Chapter 11 proceedings, I am certainly grateful for the opportunity to have appeared in front of your Committee, and for the thoughtfulness and consideration which you and the other members of the Committee and staff showed at that time. My responses to your questions follow.

Question 1:

You stated that Kaiser isn't paying benefits to retirees, notwithstanding the stop-gap measure enacted by Congress. Why can't the court simply command the payment of benefits, as intended by the law? Doesn't the court have enough weapons (e.g. contempt or other sanction) to ensure that the policy of Congress is carried out?

Answer 1:

Our analysis leads us to believe that the stop-gap measure is too risky for us to employ against Kaiser at this time. The stop-gap measure, unlike S-548, is inflexible -- it simply says that the Debtor must continue to pay the benefits. The stop-gap statute does not appear to give the Court any discretion, although the legislative history we have reviewed seems to indicate that some discretion was implied. If, however, the Court were to interpret the statute literally, the result would almost certainly be an order converting the Kaiser cases to Chapter 7, since it is clear from the reports of Coopers & Lybrand, the independent accountants for the Creditors' Committee, that the company has nowhere near the cash or assets available at this time to actually pay these benefits at their pre-petition levels.

On the other hand, if the Court were determine to it did have some discretion in this area, there is very little guidance with respect to the standard to be applied, other than S-548. Kaiser will be able to make a strong showing that in its present condition, having been depleted of its assets by prior management, it is in no position to fund retiree benefits of any kind and also preserve its estate for ultimate distribution to creditors. In addition, when contemplating medical benefits for 7,000 people, it takes a substantial amount of money to even begin to address the problem in a serious fashion. We have explored a myriad of options with the health benefits experts at Coopers & Lybrand, both in Washington, D.C. and in Dallas, and we are still wrestling with the components of an interim program which will effectively address the differing needs of these thousands of retirees. We hope to implement such a program through negotiation rather than litigation.

If, at the time of the filing of the Kaiser petition, S-548 had been in effect, I believe that either the Retiree Subcommittee or the Debtor would have brought the matter before the Court by now, with an appropriate resolution for all parties. The reason for this is that S-548 represents a balanced approach to this issue, whereas the stop-gap measure presents both sides with the prospect of an immediate Chapter 7 proceeding if it is literally enforced by the Court. The Court could certainly impose contempt or other sanctions if Kaiser willfully refused to comply with its order, but contempt cannot be imposed where the party to be charged with the contempt does not have the present ability to comply with the Court's order under any reasonable set of circumstances. The best approach, in this situation, is not to provide retirees with a weapon that they are afraid to use, but to provide them with a weapon whose power is suited to the mission to be accomplished.

Question 2:

If Kaiser converts its case to liquidation under Chapter 7, what would your clients receive in terms of benefits? What percentage of benefits owed them would in fact be paid?

Answer 2:

Conversion to Chapter 7 would probably be a disaster for retirees, for a number of reasons. To begin with, they would lose their voice in the proceedings because there are no committees authorized in Chapter 7. The trustee would take three percent of the value of the assets out of the estate, and any administrative claims in the Chapter 11 proceedings would be subordinated to the administrative claims of the Chapter 7. It may be difficult to find a trustee who would be capable of preserving the assets of the estate, particularly any going concern values, because of the difficulty of continuing the operations for any length of time in a Chapter 7 context. There would be little, if any, negotiating leverage with a Chapter 7 trustee. Retirees would probably lose the argument that post-petition medical benefits were costs of administration, and would therefore be subject to dilution by other unsecured creditors. There could be no payment, absent extraordinary circumstances, to retirees of any kind prior to the complete liquidation of the estate and the general distribution of final payment to all creditors. Traditionally, Chapter 7 trustees tend to settle litigation brought by the Debtor or creditors for a very small percentage of what parties more directly affected by that litigation would ordinarily accept. While creditors have a voice in the court approval process of any compromise of controversy, if the settlement falls within a "range of reasonableness" it will be approved by the Court. Some of the major assets of Kaiser Steel are claims which the estate has against former management, shareholders, and possibly lenders. Defendants in similar cases traditionally applaud the appointment of a Chapter 7 trustee as plaintiff in the case for these reasons. The only benefits which Kaiser retirees could expect to receive in a Chapter 7, prior to a distribution from the liquidated estate, would be those pension benefits guaranteed by the PBGC. The ability to negotiate for any further or interim benefits would, in all probability, be gone.

Beyond the payments by the PBGC, retirees would be paid a pro rata share of their general unsecured claims against the estate. Their recovery would depend on the size of their claims as they relate to the total amount of claims against the estate, and the cash which was generated by a Chapter 7 trustee in a liquidation. Based upon the analysis conducted by Coopers & Lybrand, we would not expect the percentage of recovery by retirees in a Chapter 7 proceeding to exceed 15 percent, and even that figure may be optimistic.

Question 3:

How long would the liquidation process take in terms of distribution of benefits to retirees?

Answer 3:

In order to estimate the length of the liquidation process, it is necessary to understand the asset structure of Kaiser Steel. The principal assets of Kaiser are its coal properties, the remaining assets of the steel company, including the abandoned Fontana steel mill and smaller facilities in California. and claims which Kaiser has against its former shareholders and management arising from a leveraged buyout and certain transfers to insiders, subsidiaries, and financial institutions which occurred over the past several years. Many of the physical assets are pledged, such that secured debt may have to be paid prior to any return from sale proceeds to the general estate. The Fontana mill site will be subject to EPA clean-up costs in an amount estimated to exceed $35,000,000. Although hundreds of millions of dollars were paid out by the company to shareholders and other parties prior to the bankruptcy proceedings, it is impossible to estimate to any reasonable degree the amount of recovery which may be made through the claims which Kaiser has against these entities at this time. In a Chapter 7 liquidation, I think creditors would be looking at between two and six years before they could expect a distribution.

Question 4:

Would you support -- as an alternative to S.548 -- an approach that requires companies to fund retiree health benefits in advance, through a statute similar to ERISA, to guarantee that benefits will be available even if the company is liquidated?

Answer 4:

We would support, in theory, a statute similar to ERISA which required retiree health benefits to be funded in advance so that funds would be available even if the assets were stripped from the rest of the company and/or it was liquidated. In many situations, enhanced retiree benefits seem to have been adopted by labor and management as an alternative to rising wages and costs in an effort to stay competitive. Of course, implementation of an ERISA-type system with its federal guarantee would impact the fortunes of the national exchequer in adverse ways. However, this solution may be more effective in addressing the problem in the long run. It would also have the effect of substituting a federal agency for a retiree subcommittee in bankruptcy proceedings. The problem we have in Kaiser, which really cannot be addressed at this late date, is that the cubboard is largely bare. This appears to have been the result of both Henry Kaiser's largesse in promising more than the company could deliver (in an unforeseen declining market) and of shareholders taking the assets out of the estate in the form of dividends without making a provision for the payment of the retiree obligations. An ERISA-type statute would, if properly structured and administered, make it much more difficult for a company to create false expectations in its retirees, and then leave them unprovided for when, as a result of the company's promises, the retirees have become completely dependent on the lost benefits. However, in cases where benefits are unfunded and unguaranteed, or which would not fall within the scope of such ERISA-type legislation, we believe that the approach taken by S.548 is still essential to protect the rights of the parties who stand to be most dramatically injured by these situations. Because it is my opinion that as the nature of our economy changes we will continue to see more and more Kaiser-type dislocations (as our population ages as well) it is my view that a combination of these measures should be implemented, together with some of the other measures which I discussed at the hearing, including the imposition of criminal sanctions for intentionally or recklessly placing the assets of a company beyond the reach of creditors such as retirees.

Please let me know if I can provide you with any further information. Again, thank you for your consideration of our views on these matters.

Sincerely,

for

Carl A. Eklund

CAE:keg

cc: Retiree Subcommittee
Leon Marcus
Michael Katch
David Furgason
Craig Christensen

Senator **Heflin**. Thank you, gentlemen.

Let me first ask you, Mr. Eklund, I gather that the retirees of Kaiser Steel have not sought enforcement of the stopgap measure passed by the 99th Congress because you feel the company may file a chapter 7 bankruptcy, which is complete liquidation. If that is the case, are you not concerned that this legislation, if passed, might have the result of increasing the potential of the filing of chapter 7 liquidation and thus, no benefits?

Mr. **Eklund**. Yes, Senator, that is a real concern. As soon as the bankruptcy is filed, there is a lot of hurt, there is a lot of harm that goes on and there is a temptation for retaliation.

There was a lot of discussion that we should file for Metzenbaum relief immediately but, as you have just pointed out, that could be self-destructive in our case, where there are not enough assets to maintain all the provisions of the benefit.

You absolutely are correct that it does bring us to the brink of disaster, but it is a disaster for everyone. If a chapter 7 is filed, management is removed and a trustee replaces them, so management has to also weigh whether they want to go into a chapter 7. If a chapter 7 is filed, the retirees' voice is even more silent, because there is no creditors committee to speak for them, so the retirees must also weigh heavily whether a chapter 7 is a proper alternative action.

What we have now, because of Metzenbaum, because of the new power, we have forced negotiations and you will hear from Kaiser Steel management later on today, but we are in daily communication, we are trying to hammer out a solution that probably no one is going to be happy with, but this legislation forces that to be done on a daily basis, and so I think it must be continued.

There are no easy solutions when the company is no longer factually able to pay these benefits. We must work with a scarceness, a lack of resources, and your bill forces those parties to get together because if we do not it is harm for both sides.

Senator **Heflin**. Mr. Heisler, are you a member of the union?

Mr. **Heisler**. No, sir, I am not.

Senator **Heflin**. All right. Now, the people that you represent, are they members of the union?

Mr. **Heisler**. Not any of the people in REBCO, with the exception of some who may have joined. Basically, Senator, our group is composed of retired salaried people. There may be some who are union members who have joined our activity and contributed to it. They basically would be very much in the minority, though.

Senator **Heflin**. Now, does the present or proposed bill adequately represent the nonunion retirees; and if you do not think so, how do you suggest that that be approached?

Mr. **Heisler**. Mr. Chairman, in our full statement which we gave to you there are several recommendations made in the latter part of the statement for some small alterations to the bill, but basically we feel the bill as constituted and including salaried retirees, is a great step forward for what we are looking for.

Senator **Heflin**. Senator Metzenbaum?

Senator **Metzenbaum**. I just have a couple questions of Mr. Eklund.

Mr. Eklund, how many retirees are currently left without health and life insurance benefits, and what is the value of their claims at this point?

Mr. **Eklund**. Senator, we represent approximately 7,000 retired employees. Many of them had converted to Kaiser Permanente prior to the filing of the bankruptcy. To the best of our knowledge, today there are approximately 1,500, possibly 1,200 that do not have major medical coverage today. There is also not being paid today death benefits, and that is of extreme concern to us. There were 10 deaths in March, and one of the proposals that we are attempting to thrash out as a compromise is seeing that those death benefits be paid.

The other major concern is LTD, long-term disability for salaried employees. Those people are in terrible need of assistance. We are trying to see if those benefits can continue. Then there is a very bad situation because the pension for the hourly employees is soon to be terminated and that is going to take away the money that they are using to pay for their medical benefits now. All this is coming crashing down on the retired people. At the same time if they can get any medical benefit, it is going to be greatly increased, plus the PBGC is out there with a claim as a priority above them. This is the worst of all possible conditions.

Senator **Metzenbaum**. Is Kaiser operating now?

Mr. **Eklund**. Only Kaiser Coal, which is a separate company, is "operating."

Senator **Metzenbaum**. The steel company is not operating at all?

Mr. **Eklund**. The mill has been shut down for a couple of years, yes, sir.

Senator **Metzenbaum**. And how much in other unsecured debt does Kaiser have?

Mr. **Eklund**. In unsecured debt, it is relatively minor, like $40 million, compared to the claims of the retirees. When I say that number, that excludes PBGC, which is a tremendous, maybe in the hundreds of millions of dollars, $200 million out there.

Senator **Metzenbaum**. Is the coal company making any profit?

Mr. **Eklund**. We have been told by the debtor at best the coal company is break-even.

Senator **Metzenbaum**. Did the retirees accept a cutback in medical coverage 3 or 4 years ago?

Mr. **Eklund**. Yes, a group in 1984 accepted a cutback. There are various groups of retirees that have different benefits, that is correct.

Senator **Metzenbaum**. I have no further questions. Thank you very much. I appreciate the support of both of you for this measure.

Mr. **Eklund**. Thank you, Senator.

Senator **Heflin**. Let me ask either one of you who wants to answer, I suppose there is an underlying problem and, in effect, what is forcing all the steel companies to have to go into bankruptcy? We lose sight, I suppose, of the problem that nobody has done anything about, and that is the question of imports. Do either of you want to comment on that? And the dumping and other things of this sort—if either one of you want to comment on that, I would be glad to hear it.

Mr. **Heisler**. Mr. Chairman, I believe Bethlehem Steel for years has been working here in Washington to get better teeth in trade legislation which would give a fair shuffle to the domestic steel companies as far as competition from foreign steel is concerned. I am not an authority on the subject, but I truly believe that many of the steel products that come in here from foreign countries are coming in at a price cheaper than what we can produce here in the United States simply because the government of that country supports that basic industry. This has been well documented, I am quite sure in many of the hearings that have established the trade bills that we have today. Our cocounsel, Mr. Davis, was very active at one time in putting together the trade laws as they exist today, and it has been an uphill battle.

Those are my feelings on it and that is one of the reasons why the Bethlehem Steel Corp. is in the position that it is in. When you talk about the cost of continuous casters and other things to modernize our steel industry, they are gigantic investments compared to other corporations, normal run of business. And the fact that we have had to make these in order to modernize, in order to make a better product at a cheaper cost, and at the same time we are competing in the marketplace here in the United States against steel coming in from foreign countries that is basically subsidized by their countries, it has been a very tough road.

Mr. **Eklund**. Mr. Chairman, I would like to comment briefly on that. Kaiser Steel had another problem that exacerbated where we are today and that was the leveraged buyout, and on page 9, paragraph 1, I ask that the Congress consider criminalizing conduct whereby insiders take assets out of a company knowing that promises and legal obligations exist, and they are looting companies and that has occurred in Kaiser.

There are two lawsuits attempting to address this, but as you can appreciate, those are going to take years and many, many dollars if we get any realistic recovery. The leveraged buyout is every bit as evil as insider trading and I would ask that Congress address that issue.

Senator **Heflin**. Thank you, gentlemen. We appreciate your testimony. Thank you for coming.

Mr. **Eklund**. Thank you, Senator.

Mr. **Heisler**. Thank you.

Senator **Heflin**. We will next hear from Blue Cross-Blue Shield, Mr. Joseph Patchan, senior partner, and Ms. Susan B. Collins, of Baker & Hostetler. I think Judge Patchan is a former bankruptcy judge, now connected with Blue Cross; we are delighted that you are with us.

## STATEMENTS OF JOSEPH PATCHAN AND SUSAN B. COLLINS, COUNSEL, BAKER & HOSTETLER, ON BEHALF OF BLUE CROSS-BLUE SHIELD MUTUAL OF NORTHERN OHIO

Mr. **Patchan**. Thank you, Mr. Chairman.

Mr. Chairman, Senator Metzenbaum, members of the committee staff, as the chairman has stated, my name is Joseph Patchan. I am a lawyer and practice as a senior partner at the Baker and

Hostetler law firm. I am chairman of the bankruptcy law area of the firm and have specialized in bankruptcy law for about 30 or more years, including 6 years as a bankruptcy judge.

With me is Susan B. Collins, my partner at Baker and Hostetler. Mrs. Collins has specialized in bankruptcy law work for 13 years and coordinates the bankruptcy work in our Cleveland office.

We appear in a dual capacity, as bankruptcy lawyers and as representatives of Blue Cross and Blue Shield of Northern Ohio. As bankruptcy lawyers, we support the goals of S. 548. Blue Cross and Blue Shield also support S. 548.

We disagree with those who have asserted, particularly at your prior hearing on April 1, that the Bankruptcy Code is no place for assurance of health and welfare benefits to employees and retirees. Bankruptcy law historically has been regularly amended to reflect economic and social developments of our Nation.

Our paper recites some of the various times in the past that bankruptcy law has been amended to meet public policy and economic needs. And as this committee is well aware, most recently family farmers have been accorded special protection in bankruptcy law.

Priority provisions in the Bankruptcy Code specify those creditors which Congress has recognized need special protection—wage earners, farmers, fishermen, and indeed the Government itself.

S. 548 follows the historic pattern of bankruptcy law design by placing retirees among those to be protected. We are now seeing something new in bankruptcy law use. The Bankruptcy Code does not require that a company be insolvent to obtain bankruptcy law protection.

Major companies are now resorting to bankruptcy as a business tool to meet particular circumstances. Johns Manville filed to avoid asbestos litigation; A. H. Robins filed to avoid Dalkon Shield litigation; Texaco to avoid the impact of the Pennzoil judgment. These large companies and others have gone into bankruptcy fully operational. Their shares continue to trade on the stock market. Indeed, there is active interest in their stock.

Congress should be ready and able to respond to the tactics of those who use the bankruptcy process as a business strategy, particularly when any resulting harm warrants redress. The LTV case has highlighted the needs of retirees and employees in bankruptcy cases. The current code, as you have heard, is being interpreted to require termination of retiree and employee benefits.

Retirees and employees dependent on a debtor corporation for health, life and accident benefits deserve special protective treatment during bankruptcy. Retirees are not the same as other creditors. They have no ongoing business relationship with the debtor company, no potential of recouping losses by dealing with other companies, no bargaining power, nor ability to wait for a payout, and sometimes little ability, if at all, to replace health benefits.

For retirees, the lack of health insurance or its interruption can be a personal catastrophe. We agree with the proponents of S. 548 that the legislation is needed to fill a gap in the present law and that the need is critical.

Issues concerning potential constitutional problems if S. 548 is to apply to pending cases have been raised by businesses at the April

1 hearing. Our paper cites decisions which make clear that the statute meets constitutional tests. We submit that it is essential that this statute apply to pending cases.

Apart from the extent of sheer misery which would result from a cutoff of benefits of the thousands of retirees and employees involved in the cases now before the courts, competitive considerations dictate that if this legislation is not made retroactive it will be competitively advantageous to those who file before the effective date of the law. If this law is not made applicable to pending cases, the companies already in bankruptcy will receive a windfall benefit through the shedding of retiree responsibilities.

Mr. Chairman, I see that the red light is on and I will stop at this point except to state that Mrs. Collins and I would be delighted to respond to any questions that you may have.

Thank you.

Senator HEFLIN. Bless you. [Laughter.]

Ms. Collins, are you going to testify?

Ms. COLLINS. I will be happy to answer questions. He rarely lets me talk in public. [Laughter.]

Senator METZENBAUM. We will have to speak to the ERA about that. [Laughter.]

Senator HEFLIN. The National Blue Cross, as I understand it, has offered some technical amendments to strengthen the bill, one of which would insure that there would be no break in the payment of benefits. Based on your experience with LTV, could you please explain to me how a gap in the payments would occur and how the proposed amendment would resolve this problem?

## STATEMENT OF SUSAN B. COLLINS

Ms. COLLINS. Mr. Chairman, in order to understand the nature of Blue Cross' relationship to LTV and the gap, it is necessary to explain how LTV provided for payment of health benefits.

LTV and many other large companies have elected to provide health insurance benefits to their employees on a self-insured basis. Presently, approximately 35 percent of all private health benefits are self-insured by industry. Instead of insuring their hospital claims and paying an insurance premium in advance, these companies are paying claims from their current cash flow. These self-insured companies then employ traditional health insurance companies like Blue Cross to administer the health benefit plans.

When one of these companies files a bankruptcy, there are many claims which are not as yet presented to or paid by the employer. Blue Cross, as the administrator, does not insure these claims. If the employer refuses to pay the claims, they will eventually be returned to the hospitals and billed to the retiree or the employee.

In the LTV case, $35 million of such claims have been refused payment. The amendments that we have drafted to the present legislation would cover both the self-insured as well as the third-party insured companies to insure that that stream of claims in the health care system from the hospital to the employer would be reimbursed by the debtor company and not left to the employee to deal with.

Senator **Heflin**. Is there anything like was suggested earlier, I believe by Mr. Eklund, such as having a 90-day period before the entry into the chapter 11, is there anything of that nature that would interrelate to what you have told us?

Ms. **Collins**. Mr. Chairman, because of the way the system works, in LTV's case, there are 30 Blue Cross companies across the Nation which provide claims processing to LTV employees. When an employee goes in the hospital, he may not emerge for a year if he is seriously ill. At that time, the claim is then submitted to the local Blue Cross, be it Florida, IL, and it is processed at that point by the local Blue Cross. From there, once that local Blue Cross is sure that the employee or retiree was eligible for the benefit, it pays the hospital and submits the claim to the control plan Blue Cross which at the time of the filing was Blue Cross of Northern Ohio. It is then processed for various levels of benefits and finally submitted by magnetic tape to the employer.

That process can take up to 2 years or more, so that by accident of timing one employee may have his claim paid by the company very quickly and another, because he lives far away or because he was in the hospital a long time, may not have his claim paid and that seems to us to be inequitable.

Senator **Heflin**. Senator Metzenbaum?

Senator **Metzenbaum**. To what extent is Blue Cross a creditor of LTV at the present time?

Ms. **Collins**. Blue Cross is the control plan for all of the Blue Crosses that provide a claim processing to LTV, has $35 million of hospital claims that have been refused by LTV.

Senator **Metzenbaum**. That is just in Ohio?

Ms. **Collins**. Well, that is for all the Blue Crosses, all 30 Blue Crosses.

Senator **Metzenbaum**. All 30 Blue Crosses.

Ms. **Collins**. As the control plan, it has submitted a proof of claim for that amount, but the system will spread that loss among all the Blue Crosses and they will then in turn return those claims to the hospitals as unpaid by the employer and the hospitals I assume will bill the employee or the retiree and if they do not pay then they will sue them.

Senator **Metzenbaum**. Let us get that point straight. If Blue Cross does not get paid, then you are saying that it will revert to the hospitals, the hospitals will then bill the individuals directly.

Ms. **Collins**. Exactly.

Senator **Metzenbaum**. Is that what you are saying?

Ms. **Collins**. Yes.

Senator **Metzenbaum**. What impact would S. 548 have on that situation?

Ms. **Collins**. The way it is presently drafted, those claims would not be covered. We have proposed amendments to cover the claims that are in that Blue Cross pipeline at the time the company goes into bankruptcy. Without it, those claims would not be covered by S. 548.

Senator **Metzenbaum**. What portion of the Blue Cross claim comes out of Cleveland and what portion comes out of the Youngstown area?

**Ms. Collins.** Northern Ohio was approximately 60 percent of all of the LTV employee and retiree claims.

**Senator Metzenbaum.** Lorrain, Cleveland, Youngstown?

**Ms. Collins.** Yes, sir.

**Senator Metzenbaum.** So we are talking about maybe $21 million?

**Ms. Collins.** Exactly.

**Senator Metzenbaum.** Thank you very much.

Mr. Patchan, it is good to see you again, sir. It is nice to have you with us, Ms. Collins.

**Mr. Patchan.** Thank you.

**Ms. Collins.** Thank you.

[Submissions of Mr. Patchan and Ms. Collins follow:]

Statement Of

JOSEPH PATCHAN, ESQ.
SUSAN B. COLLINS, ESQ.

BAKER & HOSTETLER

On Behalf Of

Blue Cross and Blue Shield Mutual of Northern Ohio

## INTRODUCTION

My name is Joseph Patchan, and I am the chairman of the bankruptcy practice at Baker & Hostetler, a national law firm with 350 lawyers. I have practiced in the bankruptcy area for the thirty years, including six years as a bankruptcy judge. A copy of my resume is attached to this statement.

Appearing with me is Susan B. Collins, my partner at Baker & Hostetler. Mrs. Collins has specialized in the bankruptcy practice for thirteen years and coordinates our practice in the Cleveland office.

We are appearing in our dual capacity as members of the bankruptcy bar and as representatives of Blue Cross and Blue Shield Mutual of Northern Ohio. As bankruptcy lawyers we support the goals of S. 548. Blue Cross and Blue Shield Mutual of Northern Ohio ("Blue Cross Ohio") likewise supports S. 548.

The National Association of Blue Cross and Blue Shield Plans ("National Blue Cross") has written to Senator Metzenbaum to express its support of this legislation as well (copy attached). In its letter, the National Blue Cross has offered certain technical amendments to strengthen the Bill. Blue Cross Ohio supports those amendments.

## I. THE LTV CASE.

Blue Cross Ohio specific interest in this legislation arises from its role as the administrator of the LTV Steel hospitalization plan at the time of the LTV bankruptcy. Blue Cross Ohio became involved with the problems of LTV's employees and retirees on July 17, 1986, when LTV Steel met with Blue Cross

Ohio and told it to stop paying retirees' hospitalization claims immediately. In addition, LTV told Blue Cross it would not honor any claims of either employees or retirees which had already been processed and paid by the Blue Cross system. To this day, $35 million of these LTV employee and retiree claims have not been paid by LTV.

As more and more large companies elect to provide health insurance benefits to their employees on a self-insured basis, the problems retirees and employees face in the LTV case will surface in many other industries. Instead of insuring their hospitalization claims and paying an insurance premium in advance, companies are paying claims from their current cash flow. By doing so, these companies save dollars in the short term because they avoid the cost of the state law requirements for the funding of reserves with which insurance companies must comply.

These self-insured companies then employ traditional health care insurers like Blue Cross to "administer" their health benefit plans, thereby creating the impression among their employees that they have real health insurance. This is what LTV did. In these arrangements, all that the employees really have is a month-to-month promise by their employers to pay their health care bills. The liabilities created by these health benefits are not accrued on the companies' financial statements as their employees get hospital care. These costs are huge "off balance sheet" liabilities, which, if recognized, might force the business world to analyze these companies differently.

LTV has used the Bankruptcy Code as an excuse to refuse to meet its promises to its employees and retirees. We believe that the Bankruptcy Code should not be used as a tool to refuse selectively to pay some creditors, especially those as vulnerable as the retirees.

Various witnesses before this Committee, including some bankruptcy lawyers, have urged this Committee to slow down or to forget this legislation altogether. They have stated that the

Bankruptcy Code is not the place for "social" policy. Our bankruptcy law is intended to be the source of both a fresh start for debtors and fairness and equity to creditors.

## II. THE ROLE OF BANKRUPTCY LAW AS ECONOMIC/SOCIAL LEGISLATION.

Congress has often amended bankruptcy laws to meet the needs of debtors and creditors, and to correct short-comings which are the result of economic or social developments. When companies began to use bankruptcy law to break union contracts, Congress reacted by adding Section 1113 to the Bankruptcy Code (11 U.S.C. 1113) which provides strict limitations for rejection of collective bargaining agreements by chapter 11 debtors. Most recently, family farmers were given special consideration with new bankruptcy provisions. At various times in the past, railroads and municipalities have been accommodated by amendments to the bankruptcy law as it became apparent that public policy required reorganization relief to be available because of the social and economic impact upon the country and upon people involved with those entities.

The bankruptcv statute has long reflected Congress's judgment about which debts have the greatest social significance. For example, debts for alimony, and maintenance and support cannot be discharged, nor can debts for taxes, debts incurred by fraud, debts for luxury goods, debts for drunk driving, debts for willful and malicious injuries, or debts for student loans. The list of nondischargeable debts contained in 11 U.S.C. § 523 reflects Congress' view that the social importance of some debts is a valid ground to refuse to permit them to be forgiven.

Similarly, Congress, because of social and policy needs, has provided for priorities which require payment of some creditors before others in a bankruptcy case. Wage earners, farmers, fishermen, and, indeed, the government itself are accorded priority status over other creditors. Each class entitled to priority status in bankruptcy was selected because

Congress recognized that a class is particularly in need of protection.

The bill now before this Committee follows the traditional pattern of bankruptcy law development and design: recognition of a serious need to protect a substantial group of people. Retirees require protection because they cannot afford to suffer either interruptions or delays in health care benefits to which they are entitled. The bill would grant a priority for health, accident, and life insurance benefits, but not unfunded pensions or other benefits.

## III. RECENT INNOVATIVE USES OF BANKRUPTCY AS A CORPORATE STRATEGY.

The Bankruptcy Code does not require that a company be insolvent to obtain bankruptcy law protection. Major companies are now resorting to bankruptcy as a corporate survival strategy, often to meet a particular circumstance apart from the general business or financial affairs of the company. Continental Airlines filed to avoid a labor contract; Manville filed to avoid asbestos litigation; A. H. Robins filed to avoid Dalkon Shield litigation; LTV filed in part to avoid obligations to retirees; and Texaco filed to avoid the Pennzoil judgment.

Bankruptcy law has historically been an expanding concept. At one time, it was a criminal law applicable only to merchants and traders. The uses and application of the law have continually been modified to reflect changes in the Nation's economic history. Since the stigma heretofore attached to bankruptcy filings has been lessened and the bankruptcy court is no longer a gloomy place to be feared, we will undoubtedly see more solvent companies resort to bankruptcy to resolve a particular liability or other corporate problem.

Congress regularly examines bankruptcy laws to assure it stays abreast of the latest corporate strategies and economic conditions. Congress should be ready and able to respond to the tactics of those who use the bankruptcy process when the resulting harm warrants redress.

A century and a half ago, Senator Thomas H. Benton, interpreting the bankruptcy clause of our constitution (Article I, Section 8, Clause 4), stated to the Senate:

> [W]e are to use our granted powers, according to the circumstances of our own country, and according to the genius of our republican institutions, and according to the progress of events and the expansion of light and knowledge among ourselves.

Congressional Globe, 25th Cong., 1st Sess. 128 (October 12, 1837).

## IV. SEPARATE TREATMENT FOR RETIREES AND EMPLOYEES IN THE BANKRUPTCY CODE IS BOTH NECESSARY AND APPROPRIATE.

The progress of events now calls for protection of retirees and employees of debtor companies. They should be protected at a minimum to the extent of the health benefits for which they have worked. That protection is properly and best treated as proposed by S. 548 now before the Committee.

We have cited some groups which have been given special consideration in bankruptcy provisions in the past. Each of these groups has been given special consideration because equity and public policy required it. Retirees and employees dependent on a debtor corporation for their health, life, and accident benefits also deserve special, protective treatment. They have many characteristics that render them far more vulnerable to the chapter 11 bankruptcy process than the normal trade creditor. In addition, the equities require special consideration for retirees and employees.

What are some of the differences between retirees and other creditors? The normal trade creditor often has an ongoing relationship with the debtor in possession as a trade creditor or a lending institution. Business creditors have the potential of recouping their past losses in part from their future financial dealings with the debtor and their other customers. This ongoing relationship also gives them bargaining power in their current financial relationships with the debtor. In general, trade and lending institution creditors choose voluntarily to extend credit to the debtor based on their appraisals of the risks involved. They are sometimes in a position to demand security if sufficiently uncomfortable. Such creditors can calculate at any given time the specific dollar amount for which they are at risk, and they can plan accordingly.

In contrast to other creditors, retirees and employees have few places to look for help other than the debtor corporation and have little or no bargaining power. They do not make a conscious choice to extend credit to a company based on an assessment of the risks involved, nor are they in a position to demand security for their interests. Retirees are not in the job market and thus cannot recoup their losses or replace their benefits through other activities in the marketplace or by obtaining different jobs.

The prospect of some future distribution to unsecured creditors is of little immediate benefit to retirees and employees, particularly in a large case which can easily go on for years. Older or infirm retirees may not live long enough to see such a distribution; and, by that time, funds to replace their health and life insurance are of little help. Retirees will find it exceedingly difficult to borrow now to meet their immediate needs until the day when they might obtain that distribution. Moreover, the financial cost to them of the loss of coverage will vary widely depending on each retiree's individual circumstance.

Most significantly, the health and insurance benefits addressed by S. 548 are benefits that may be completely unavailable to retirees who most need them. For others who attempt to buy on an individual nongroup basis, they will be far more expensive. What insurance they do obtain may not cover current afflictions and may leave a gap between the start of coverage and the date of termination of the employers' group insurance. For retirees, the lack of health insurance can be an economic and emotional catastrophe.

In short, the hardships and burdens to retirees of taking away their health and insurance benefits are far disproportionate to the consequences to creditors in general, and retirees are in a far worse position either to protect themselves against the eventuality of the bankruptcy or to find alternate ways to cope as a result of it. Consequently, specific bankruptcy legislation to address their unique situation is not only justifiable but essential.

The problem is likely to get worse, instead of better, absent this legislation. In the last few years, numerous major companies have gone into chapter 11 reorganization, with the latest being Texaco, Sharon Steel, and Phoenix Steel. Even those debtors that have no desire to cease paying retiree benefits are forced to discontinue them under current law. You have heard the testimony of Mr. Robert G. Watts, Executive Vice President of the A. H. Robins Company, who testified that, after going into chapter 11, Robins was advised by its bankruptcy counsel that it not only could discontinue retiree benefits, but must discontinue them, because, under the Bankruptcy Code, such benefits are viewed as unsecured, nonpriority prepetition debts. A. H. Robins was thus forced into a posture that it considered to be both unreasonable and inequitable. The advice of A. H. Robins' counsel was not wrong, but the current law is. The entry of a viable company into chapter 11 should not in and of itself produce such a devastating result for its retired workers and employees who rely on the company's health and insurance benefits.

Further, as other industries face economic downturns, and as companies turn to chapter 11 for increasingly creative purposes, we are likely to see more cases like LTV in which a company seeks the protection of a bankruptcy court in order, among other things, to free itself from the many years of unfinanced promises that it made to its swelling numbers of retired workers. Therefore, current protection of the retired and existing employees is critical.

## V. THE STATUTE CAN AND SHOULD BE APPLICABLE TO EXISTING BANKRUPTCY CASES.

Other witnesses have raised the issue of potential constitutional problems if this legislation is made applicable to pending cases in chapter 11. Such arguments and warnings go back to our earliest bankruptcy laws, having been raised with every change in this country's bankruptcy laws. More than 80 years of constitutional case law, starting with the 1902 case of Hanover National Bank v. Moyses, 186 U.S. 181, 188 (1902), amply refutes them.

As stated in New York Credit Men's Adjustment Bureau, Inc. v. Goldstein & Co., 276 F.2d 886, 888 (2d Cir. 1960), a case involving a postpetition congressional bankruptcy amendment changing the order of priority of creditors, "Congress has the power to enact legislation rearranging the order of priorities to be observed in the distribution of a bankrupt's property and to apply such a law to proceedings pending at the time of its enactment, without violating the Fifth Amendment." This power is recognized by numerous cases. See, e.g., Carpenter v. Wabash Railway, 309 U.S. 23 (1940) (applying a congressional amendment that was enacted during the pendency of a railroad receivership to give priority to claims for personal injuries to employees); Coin Machine Acceptance Corp. v. O'Donnell, 192 F.2d 773 (4th Cir. 1951) (postpetition bankruptcy amendment applied to give preferential treatment to trust receipts); City of Chelsea v. Dolan, 24 F.2d 522 (1st Cir. 1928) (postpetition bankruptcy amendment applied to give wages priority over taxes); and In re Garland Corp., 6 Bankr. 456 (D. Mass. 1980) (holding that postpetition loan could constitutionally be given priority pursuant to § 364(c)(2) of the Bankruptcy Code).

It is not only constitutional to apply this statute to pending cases, it is essential to do so. With large companies like LTV, Texaco, and A. H. Robins currently in bankruptcy, the amount of sheer human misery that will result from leaving their tens of thousands of retirees and employees suddenly bereft of the insurance benefits that are often their sole bulwark against financial and medical disaster is sufficient reason to make the bill applicable immediately.

Competitive considerations also dictate that this legislation apply to pending chapter 11 cases. If the legislation is not retroactive, it will only be advantageous to those who have filed prior to the effective date. Steel is an industry presently under economic siege. If LTV, Wheeling-Pittsburgh Steel, Kaiser Steel, and now Sharon Steel and Phoenix Steel are permitted to avoid the costs of their retiree benefits, others in the steel industry would have to consider filing chapter 11 cases immediately to stay competitive. Companies in other industries under competitive pressure might also be forced to consider filing petitions promptly.

## IV. IMPACT ON THE CHAPTER 11 PROCESS.

The proposed legislation, if adopted, will give priority in bankruptcy cases for the cost of ongoing health, accident, and life insurance benefits. The bill also creates a separate class of creditors for purposes of voting on the reorganization plan. In addition, this legislation has a moderating feature which permits the amount of benefits to be reduced by the court after considering the financial circumstances of the debtor.

The prophets of doom opposing this legislation predict that available credit will shrink, fewer chapter 11 cases will succeed, and the process will last forever. Every legislative proposal affecting credit, e.g., Truth in Lending, is answered with warnings of lessened credit. Credit shrinkage was predicted when EPA superfund laws were enacted, but the credit market has adjusted, not shrunk. Since most bank loans are secured by collateral, S. 548 should not materially affect bank creditors. Trade creditors are affected by market competition, selling pressures, and credit ratings, not by regard for their priority in chapter 11.

Enactment of this bill would cause lenders and suppliers to consider retiree and employee obligations in assessing creditworthiness. As a result, this legislation may have the salutary effect of forcing employers to fund fully their obligations to employees and thereby relieve creditors or the government of substantial costs.

The critics say that fewer chapter 11 cases will succeed if S. 548 is enacted. The chapter 11 cases that will not succeed are the chapter 11 cases that are filed for the sole purpose of avoiding the payment of the benefits that were promised to workers. Legitimate chapter 11 cases will not fail. The bill gives the bankruptcy court full power to modify benefits when doing so is necessary for a successful reorganization.

Critics also predict that the process of plan negotiation will be impeded by the designation of the retirees as a separate class. The bill does give the retirees a voice in the plan and a seat at the negotiating table, where they had none before. The addition of a new party to the bargaining table may add to the complexity of the process; but any problems are more than offset by an unexpected benefit of this bill for the entire chapter 11 process for the debtor will no longer be able to tarry on its way to the table. It will have to move promptly toward the formulation of a plan after filing the case. In spite of limitations within the Bankruptcy Code, debtors regularly find it in their interest to delay work on the reorganization plan. The costs attributable to the ongoing needs of the retirees will exert desirable pressure on the debtor, on creditors, and even on the court to press for prompt attention to a plan, with the result that chapter 11 cases should be concluded more expeditiously, instead of the three, four, or more years now commonly expected.

## VI. CONCLUSION

One in every six elderly people in the United States is receiving a portion of his or her health coverage from an employer. In 1983, at least 6.9 million retirees and their dependents were covered by private health insurance, provided primarily by large companies. Medicare has not met the complete needs of people over age 65, and the gaps are growing. Medicare is not available to retirees under age 65--including many of LTV's retirees who were induced to take early retirement by benefits such as company paid health, accident, and life insurance benefits. These benefits are not afforded the protections that ERISA mandates for pension benefits and are not insured by the Pension Benefit Guaranty Corporation.

Senate Bill 548 is a fair compromise for retirees. It does not mandate benefits; it merely requires that chapter 11 debtor companies provide them, if economically feasible, on a priority basis to their retirees. The court can modify the benefits if there is insufficient money to pay for them.

This country is faced with a population, the median age of which is rising steadily. Congress must address the rights of retirees now, so that equitable treatment is afforded now and into the future. To delay addressing the problem will result in saddling our children with the cost of solving a major social and economic problem. We cannot allow corporations to reorganize at the expense of the security of our elderly.

Baker & Hostetler, as counsel for Blue Cross and Blue Shield Mutual of Northern Ohio, appreciates this opportunity to speak in favor of S. 548.

**Blue Cross**
and
**Blue Shield**
Association

Bernard R. Tresnowski
President

676 North St. Clair Street
Chicago, Illinois 60611
312/440-6010

April 16, 1987

The Honorable Howard Metzenbaum
United States Senate
140 Russell Senate Office Building
Washington, D.C. 20510

Dear Senator Metzenbaum:

The Blue Cross and Blue Shield Association would like to express its support for S. 548, the proposed Retiree Benefit Security Act of 1987. We believe the bill addresses a serious shortfall in existing bankruptcy law.

Historically, no safeguards have existed in bankruptcy to protect the health and life insurance benefits of retirees. Retirees are among the most vulnerable of a company's creditors, yet currently they stand with the general unsecured creditors on the bottom rung of the Chapter 11 distribution ladder. Their benefits, considered to be prepetition claims, are subject to termination when a bankruptcy is filed. As we in the health field are aware, a bankruptcy creates hardship for all creditors, but the abrupt and unexpected termination of retiree' group medical benefits is irreparably devastating.

S. 548 provides that:

o Employers in bankruptcy could not unilaterally terminate the health, life or disability benefits they have promised retirees, whether those benefits are collectively bargained or not.

o Retirees would have a specially appointed representation in the bankruptcy case and their benefits would continue until the company and the retirees' representatives agreed upon modifying them.

o In situations where the continuation of current retiree benefits threatened the continued viability of the company, the bankruptcy court could force approval of modified benefits under a reorganization plan.

We recommend that S. 548 be modified to provide that all unpaid benefit claims are accorded the same protection provided for post petition claims. We also believe that it needs to be made clear that the obligation to continue retiree benefits is strictly an obligation of the bankrupt and not of any third party.

The Blue Cross and Blue Shield Association supports S. 548 generally as a sound legislative initiative that is urgently needed in view of the upcoming May 15, 1987, expiration of the law which temporarily extended the provision of retiree benefits for companies in bankruptcy. We believe that this legislation is directed toward a sensible and humane solution to a very severe problem.

Very truly yours,

Bernard R. Tresnowski

**May 12, 1987**

**RESPONSE TO QUESTIONS PROPOUNDED TO**
**JOSEPH PATCHAN AND SUSAN COLLINS**

**QUESTION 1**: Why is it an advantage to have third party administrators of health benefit plans at the negotiation table?

**ANSWER 1**: The Administrator of health benefit plans should be directly involved in the formulation of the reorganization plan because that party is the one most familiar with the detailed complexities of providing health benefits through a self insured arrangement. In addition, this party has the ability to estimate both present and future costs of such plans. In that capacity, this party can bring a unique degree of knowledge to the bargaining process which would not otherwise be present.

**QUESTION 2**: Aside from making retiree benefits an administrative expense, is there any way to ensure that retirees receive payment of their benefits? What does the creation of this administrative priority do to the dynamics of out-of-court workouts and Chapter 11 cases?

**ANSWER 2**: The only other way to ensure retirees are paid their benefits other than providing fully funded plans or government insurance is to provide them with a lien on the assets of the debtor. The passage of S. 548 may encourage debtors to resort to out-of-court workouts rather than filing in bankruptcy because bankruptcy will no longer provide a haven for those seeking to avoid obligations to retirees. The retirees also will have an incentive to participate in workouts because they may receive less favorable treatment from a bankruptcy judge than through such negotiations.

**QUESTIONS 3**: One interpretation of the section on interim modifications suggests that the bankruptcy judge would be required to use cash collateral to pay retiree benefits.

Can this be done? Is it legal?

**ANSWER 3**: Although the court has the power to grant the use of cash collateral, it can authorize such use only if the secured party is granted adequate protection of its interest. Adequate protection can take the form of a replacement lien on some other property. If the secured parties interest cannot be adequately protected, the cash collateral may not be used under present law. This situation is not affected by the proposed legislation.

**QUESTION 4**: The National Bankruptcy Conference recommends that Congress create a new Section 507(a)(5) priority with a defined maximum priority amount per retiree covered by a retiree medical plan.

How would you go about setting that amount given that the situation will vary dramatically from retiree to retiree.

**ANSWER 4**: As a general proposition, a fixed maximum payable to each retiree for health benefits will not meet the needs of individual retirees. People are not equally ill. Specifically, in the case of companies with self-insured health plans, use of maximum priority amounts for retirees who have incurred no health care expenses is irrelevant . For those retirees who have incurred significant health care expenses, use of a maximum priority amount per retiree would inflict considerable economic harm. In the case of companies who have obtained insured health coverage, use of a maximum priority amount per retiree is inherently defective because it fails to take account of the length of time of the bankruptcy case.

**QUESTION 5 :** How do you interpret Section 1114(h) of the proposed legislation?

**ANSWER 5:** We read section 1114(h) to mean that absent consent, payments made to a retiree during the administration of the case will not be credited to or deducted from disbursements made under a confirmed plan or be considered as a credit in regard to the allowance of a retiree's claim. The current language may, however, be confusing since it could be read as allowing a retiree to file a claim for benefits already received. We believe that its purpose could be clarified by stating it as follows:

> 1114 (h) Any modifications made to retiree benefits, pursuant to this section, are presumed to affect only those benefit expenses not yet incurred or accrued. Unless otherwise expressly agreed by the debtor and the authorized representative of the recipients of those retiree benefits, no retiree benefit claimant shall have to pay back any sums in respect of benefits already received and no plan payout in respect of benefits not yet actually received shall be reduced because of such prior receipt of benefits.

**QUESTION 6:** As you know, the proposed legislation would elevate the status of retiree benefits to administrative expenses during the pendency of the petition.

Are there other rights which should receive consideration for similar treatment?

**ANSWER 6:** We know of no matter more deserving of elevation to priority status than retiree benefits except possibly accommodating similar claims of existing employees.

Senator HEFLIN. Thank you.

Our next panel is from the National Bankruptcy Conference, Mr. Herbert P. Minkel, chairman of the Employee Benefits Committee, and Mr. Lawrence P. King, professor of law at the New York University School of law.

We appreciate your coming. Mr. King, we understand that you made a particular effort to be here today and we thank you for that.

Mr. Minkel?

## STATEMENT OF HERBERT P. MINKEL, JR., CHAIRMAN, EMPLOYEE BENEFITS COMMITTEE, AND VICE CHAIRMAN, LEGISLATION COMMITTEE, NATIONAL BANKRUPTCY CONFERENCE; ACCOMPANIED BY LAWRENCE P. KING, CHARLES SELIGSON PROFESSOR OF LAW, NEW YORK UNIVERSITY SCHOOL OF LAW, AND CHAIRMAN, LEGISLATION COMMITTEE, NBC

Mr. **Minkel**. Senator, since I have 5 minutes, I will try to be brief and quick.

The members of the National Bankruptcy Conference met in Dallas in March to consider S. 548. The conference had——

Senator **Metzenbaum**. Mr. Minkel, let me explain. The chairman and I are going to leave alternately. We have a vote on. I will go and vote while the chairman proceeds, and then I will return and preside on while he goes to vote.

Mr. **Minkel**. I understand.

Senator **Metzenbaum**. I do not want you to think I am walking out on you.

Mr. **Minkel**. The Conference has substantial problems with S. 548 in its present form. The Conference feels that legislation in this area is appropriate but feels that, notwithstanding the emotions surrounding the action of LTV and the situation of retirees in other cases, that Congress should try to back off from LTV and from Kaiser Steel and look at the problem as a more general matter.

The best way to protect retirees is to keep companies out of bankruptcy. S. 548, if it were enacted, would cause more companies to wind up in chapter 11 and they are the type of companies where out-of-court restructurings will of necessity take place because they are in the troubled industries, the old and mature industries in the United States.

If companies have to take recourse to the Bankruptcy Code, it is obviously better for retirees that the companies survive and that the assets be maximized and that as much of the safety blanket of retiree protection be preserved to the extent possible. That is not going to happen if S. 548 is enacted. There will be more liquidations.

It has been suggested that it is in the best interest of retirees that the assets of a debtor be in effect a trust fund for the funding of retiree medical benefits and that this somehow means only that greater hardship will only be visited on institutional creditors and the like.

Senator, I can assure you that I have gotten letters from retirees from all around the country whose life savings are tied up in bonds, modest amounts, but the interest on those bonds are what these people live on. They are retirees too and they are creditors of these estates. Bankruptcy has always tried to recognize the right of equality of distribution among similarly situated people, and S. 548 is a radical departure from this rule.

Let me explain briefly why this bill will change the balance. When Congress put chapter 11 together in 1976, 1977, and 1978, they tried to create a balance of negotiating strength of people out of court. The view was that if chapter 11 was evenhanded, it would keep companies out of bankruptcy by offering incentives to people to negotiate in good faith out of court.

If you create a trust fund for retirees using the debtor's assets, there is no incentive on the part of retirees to compromise their claims out of court. Now, there are cases like LTV where maybe there should not be any compromise of those claims. On the other hand, I am today working on a case in the Midwest. It is not in chapter 11. We are trying to keep it out of chapter 11, there are 12,000 retirees. There are only 4,000 current employees of this company. The company does not have the cash flow to pay the interest on its institutional debt which is secured. The secured creditors are not getting the interest today. The company is paying in excess of half a million dollars a week in retiree medical benefits, $25 million a year to the retirees, another $5 to $10 million to current employees.

That situation cannot continue for this company or this company is going to wind up in chapter 11, and the Constitution of the United States protects the rights of secured creditors. So if you were to pass a law that said the cash flow of the company goes to pay retirement benefits first and does not go to service secured debt, that law would violate the fifth amendment.

So while it is commendable to want to protect retirees, the protection has to be balanced against the rights of all the players in the troubled world of problem credits.

In Dallas the NBC considered an alternate proposal. First of all, they believe that the S. 548 as proposed does not work. There should be group treatment of retiree benefits. If you are looking to give substitute coverage, then there has to be the mechanics in place for treating a retiree group as a group. The reason I say that, Senator, is that there are 85,000 LTV retirees. A bankruptcy court cannot determine those claims on a claimant by claimant basis. It is technically impossible. It will take 20 years of a judge's time to do that. There are numerous technical imperfections which can be worked out, but you are being asked to legislate in an incredibly complicated area and the legislation by itself is not going to solve the problem. You should consider whether ERISA should apply to retirement benefits; whether employers should be permitted to make promises that they really cannot fulfill; and the circumstances under which they should fund these promises. That is not going to be done through amendments to the bankruptcy law. That is going to be done by recourse to other Federal legislation.

Thank you.

[Submissions of Mr. Minkel follow:]

# STATEMENT OF HERBERT P. MINKEL, Jr.

Before the Subcommittee on Courts and
Administrative Practice of the
Senate Judiciary Committee
April 24, 1987

Mr. Chairman and members of the Committee, my name is Herbert P. Minkel, Jr. I am appearing today before this Committee in my capacity as Chairman of the Employee Benefits Committee and Vice-Chairman of the Legislation Committee of the National Bankruptcy Conference. I am a member of the firm of Fried, Frank, Harris, Shriver & Jacobson and am the contributing editor to Collier on Bankruptcy responsible for those sections dealing with business reorganizations. Appearing with me is Professor Lawrence P. King, Charles Seligson Professor of Law at New York University School of Law and Chairman of the Legislation Committee of the National Bankruptcy Conference.

As you are aware, the National Bankruptcy Conference is a non-profit, unincorporated organization, composed of representatives of different groups who are interested in the administration of the bankruptcy laws of the United States. The Conference includes judges, full-time professors of law, and practicing attorneys who specialize in this area. There are 68 full members and 2 associate members from all areas of the country.

We are appearing today on behalf of the National Bankruptcy Conference to comment on S.548 dealing with retiree medical benefit claims in bankruptcy.

## General Statement of Principles

The failure of LTV Corporation to pay retiree medical benefits subsequent to the filing of its chapter 11 case in July of 1986 focused national attention on the effect of bankruptcy on the rights of retirees. Congress had previously enacted statutory safeguards to protect the rights of retirees to receive pension benefits notwithstanding the insolvency of a plan or plan sponsor. See Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001, et seq. In response to the LTV chapter 11 filing, Congress enacted Pub. L. No. 99-591 (November 4, 1986), effective October 1, 1986, which requires trustees or debtors-in-possession to maintain retiree medical benefits "on existing levels" until May 15, 1987. This law applies to employers paying retiree medical benefits on October 2, 1986 that had not obtained bankruptcy court approval of their plan prior to such date and to employers who file for relief under Title 11 after such date.[1]

We do not question that the special hardship that bankruptcy may impose on employees and retirees makes the protection of their pension and medical benefits an appropriate subject for Congressional action. In the case of retirees, we would urge that considerations of equity dictate equality of treatment between union and non-union retirees. See Statement of Herbert P. Minkel, Jr. and Lawrence P. King, Hearings before the Subcom. on Monopolies and Commercial Law of the Comm. on the Judiciary regarding H. R. 5238, August 7, 1986. It must be recognized, however, that the problem of large claims related to vested retiree medical benefits occurs most often in the context of large corporations in mature or declining manufacturing industries which are now functioning in a highly competitive environment. Resort to chapter 11 does not automatically assure that the debtor will be able to restructure itself in a form which can compete and survive. It simply creates a structure in which there is an opportunity for the rights of the debtor and creditors, including employees and retirees, to be reconciled and balanced so as to create a viable entity. Before legislating with respect to retiree medical benefits, we believe Congress should have the opportunity to evaluate empirical data on the magnitude of unfunded retiree medical benefits in the industrial sector and to carefully consider the potential impact which mandating the post-petition payment of such benefits may have upon the effectiveness of chapter 11.[2] Given the fact that any debtor has only finite resources, Congress should consider whether creating statutory priorities in favor of retirees with respect to medical benefits will make the out-of-court restructuring of troubled companies more difficult, force more companies into chapter 11, and undercut the effectiveness of chapter 11 as a means of reorganizing industrial debtors. Congress should further consider whether the creation of potentially massive priorities may be counterproductive to the extent that such action will make it more difficult for U.S. companies to obtain financing and to compete effectively against foreign competition as well as newly established, foreign-owned, U.S. based enterprises. We take note of an article in the March 5,

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[1] Pub. L. No. 99-591 represents an interim response to an extremely emotional hardship problem, to wit, LTV's suspension of retiree medical benefits immediately after the filing of its chapter 11 case. It is not clear that Congress intended the law to apply to chapter 7 liquidation cases since there is no mechanism in a chapter 7 case for the consensual modification of retiree medical claims. Thus, as applied to a chapter 7 case, Pub. L. No. 99-591 could be construed to require all of the proceeds of a liquidation to be used to fund retiree medical expenses prior to distribution to other creditors. Nor is it clear that the law was intended to, or could constitutionally, require the use of proceeds of a secured creditor's collateral to make the required payments. If Congress determines to extend the May 15, 1987 deadline in Pub. L. No. 99-591, it is suggested that Congress limit the scope of the bill to chapter 11 cases, protect the rights of secured creditors, and permit the bankruptcy court to order a termination or reduction in payments in respect of retiree medical benefits if the continuation of such payments will threaten the ability of the debtor to reorganize.

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[2] Currently, approximately 6.9 million retirees and their spouses are receiving employer-sponsored health insurance and an estimated 16 percent of the population over 65 received supplemental health coverage through private sector employer-sponsored retiree health programs. The Administrations's Proposal on Funding and Termination of Defined Benefit Pension Plans, U.S. Department of Labor, Pension and Welfare Benefits Administration, p.4 (Feb. 1987).

1987 Wall Street Journal concerning the disproportionately high employee medical expenses of U.S. car manufacturers when compared with such costs of Japanese manufacturers producing cars in the United States with younger work forces. Obviously such newly created enterprises do not have to cope with the additional burden of substantial retiree medical benefits. We believe that all of these factors should be carefully considered before Congress legislates in this extremely sensitive area.

Industrial companies do not make reference to the bankruptcy laws when structuring their employee benefit practices. Amending the bankruptcy laws will not address the underlying problem, namely, permitting companies to make promises to employees concerning the scope and duration of medical benefits without requiring employers to create appropriate reserves to fund the cost of such programs. The mandatory funding requirements of ERISA have sensitized employers to the reality that increases in pension benefits may impose on the employer additional annual funding obligations under ERISA. It is fair to question whether permitting a debtor to increase the scope of medical benefits without making any provision for funding such benefits constitutes sound social policy.

Congress should investigate the appropriate means of preventing employers from making promises to employees and retirees which they may not be able to fulfill. Amending the bankruptcy laws in the manner suggested by S.548 merely shifts the burden of broken promises on to the shoulders of vendors, employees, taxing authorities and bond holders. We question the fairness of this approach to the solution of a serious problem.

Creating significant priorities in favor of retiree benefits will, in time, result in the reallocation of credit away from those companies in America's industrial heartland which have large unfunded vested retiree medical benefits. The

Administration has already suggested the need to give Pension Benefit Guaranty Corporation an unlimited claim in bankruptcy for the shortfall between plan assets and guaranteed vested plan benefits and afford such claim priority status under 11 U.S.C. § 507(a)(7). We cannot over-emphasize the fact that, faced with these priorities, institutional creditors will either not lend or they will only lend on a secured basis. Restructuring secured debt in bankruptcy is considerably more difficult than restructuring unsecured obligations. See 11 U.S.C. §§ 361-364. See also In re American Mariner Industries, Inc., 734 F.2d 426 (9th Cir. 1984); Grundy National Bank v. Tandem Mining Corp., 754 F.2d 1436 (4th Cir. 1985) (payment of post-petition interest on partially secured claims). But see In re Timbers of Inwood Forest Associates Ltd., 793 F.2d 1380 (5th Cir. 1986), aff'd en banc, 808 F.2d 363 (5th Cir. 1987); In re Briggs Transportation Co., 780 F.2d 1339 (8th Cir. 1985).

S.548, if enacted, will significantly change the negotiation dynamics in out-of-court workouts and will force more troubled companies into chapter 11 by reason of the debtor's unwillingness to "risk the franchise" by granting collateral security to institutional creditors out of court. Successful out-of-court workouts are a function of stabilizing credit relationships with both institutional and trade creditors. Trade creditors lend on an unsecured basis and carefully manage the risk of loss in bankruptcy against profit margins on goods and services supplied to the debtor outside of bankruptcy. The creation of the priorities contemplated by S.548 will, in our opinion, cause the trade to run for cover in cases where trade credit could otherwise be sustained without recourse to chapter 11. We who have front line experience with business reorganizations have enormous sympathy for the pain and suffering that insolvency has on small investors, the "mom and pop" suppliers, rank and file employees and retirees. The best way to serve their needs in a problem situation is to successfully structure an out-of-court workout. S.548, if enacted in its present form, will increase the number of chapter 11 filings and will push chapter 11 debtors, which can be restructured under present law, into liquidating bankruptcy under chapter 7. We urge Congress to find a better way to address this problem.

## Status of Retiree Benefit Claims

Retiree benefits which vest upon an employee's retirement give rise to a prepetition claim if retirement occurs prior to the employer's filing for relief under Title 11 of the United States Code.[3] If such retirement benefits

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3. Welfare benefits do not necessarily vest at the time of retirement. Whether welfare benefits vest at the time of retirement is determined by reference to the agreement setting forth the retiree's entitlement to receive such benefits. If the agreement through which the benefit arises, gives the employer the right to terminate welfare benefits, such benefits are not vested. *See International Union, United Automobile, Aerospace and Agricultural Implement Workers of America and Local 134 v. Yard-Man, Inc.*, 716 F.2d 1476 (6th Cir. 1983), *cert. denied*, 465 U.S. 1007 (1984). The Sixth Circuit in *Hansen v. White Motor Corp. (In re White Farm Equpment Co.)*, 788 F.2d 1186 (6th Cir. 1986), reversed the district court's determination that there is a federal common law rule limiting the right of an employer to exercise after retirement a reserved right of termination of employee welfare benefits. 788 F.2d at 1191. The court noted that there is an expressed statutory exclusion of welfare plans from the stringent minimum vesting, participation and funding standards imposed on pension plans, ERISA §§ 201(1), 301(a)(1), 29 U.S.C. §§ 1051(1), 1081(a)(1), and also an exclusion of welfare benefits from the definition of accrued benefits in Treasury Regulations, 26 C.F.R. § 1.41(a)-7(a)(ii) (1981), promulgated under ERISA § 1053(a), 26 U.S.C. § 411.

   The Fourth Circuit in *Sutton v. Wierton Steel Div. of Nat. Steel Corp.*, 724 F.2d 406 (4th Cir. 1983), *cert. denied* 467 U.S. 1205, (1984), held that an employer may change ancillary benefits without violating ERISA.

   The power to terminate, however, has to be clearly set forth in the agreement. *See Turner v. Local Union No. 302, International Brotherhood of Teamsters*, 604 F.2d 1219 (9th Cir. 1979); *Hamilton v. Travelers Insurance Co.*, 752 F.2d 1350 (8th Cir. 1985). Any ambiguity with respect to the employer's right to terminate benefits has generally been construed against the employer. *See International Union, United Automobile, Aerospace and Agricultural Implement Workers of America and Local 784, v. Cadillac Malleable Iron Co.*, 728 F.2d 807 (6th Cir. 1984); *Weimer v. Kurz-Kasch, Inc.*, 773 F.2d 669 (6th Cir. 1985).

are unsecured, the claim arising in respect of such benefits is a prepetition unsecured claim. This conclusion follows irrespective of whether the benefits arise under a collective bargaining agreement covered by 11 U.S.C. § 1113. Section 1113 was intended to provide a framework through which representatives of collective bargaining units may negotiate the terms and conditions of employment during the pendancy of a reorganization case. It represents an effort to better harmonize the policies of the Bankruptcy Code with the policies of the National Labor Relations Act. Retirees are not members of the collective bargaining unit and the members of the collective bargaining unit can not bind retirees with respect to the modification of the retirees' rights. Since the rights of retirees accrue prior to bankruptcy, the fact that such benefits were created under a collective bargaining agreement prior to the filing date, does not alter this conclusion. Current employees are treated no differently. The wage, vacation and fringe benefit claims of employees which accrue in connection with services rendered prior to the filing date, give rise to prepetition general unsecured claims to the extent that such claims exceed the § 507(a)(3) and (4) priorities. Administrative expense claim priority under § 507(a)(1) is only available to persons providing goods and services to the trustee or debtor-in-possession after the filing date.

### Priority Status

We support the general guiding principle of the bankruptcy laws of the United States that similarly situated creditors are entitled to equality of treatment. We recognize, however, that the Code contains statutory exceptions to this rule. The administrative expense priority (11 U.S.C. § 507(a)(1)) is not an exception to the general principle in that it only arises through post-petition activities which directly benefit the estate and must be paid if there is to be post-petition administration of such estate.

The Conference has generally taken a position against the creation of priorities for prepetition claims since they undercut the Code's general policy of equality of distribution. Priorities represent a legislative determination that the hardship which bankruptcy visits on a particular group of creditors requires preferred treatment of that group. In most cases, however, preferred treatment of one group of creditors only exacerbates the hardship imposed on other creditors. The tax priority (11 U.S.C. § 507(a)(7)) subordinating the claims of creditors to the rights of the sovereign to collect unpaid taxes is a long-standing priority which is essentially unlimited in amount. Other priorities created by the Code have generally been limited in amount so as to avoid undue impact on non-priority creditors.

The limited wage and employee benefit priorities provided for in the Bankruptcy Code (11 U.S.C.§ 507(a)(3) and (4)) are designed to protect employees for amounts up to $2,000 per employee which an employer fails to pay prior to commencing a bankruptcy case. It has become quite common for a chapter 11 debtor-in-possession to seek court authority to pay prepetition wage and benefit claims in an amount up to the $2,000 priority promptly after the beginning of the case. Courts have generally authorized such payments since they do not prejudice the rights of general unsecured creditors. Thus, the existence of the wage priority permits the orderly payment of most wage claims and avoids the hardship and morale problems associated with failure to pay employees for services rendered to the debtor immediately prior to the filing of the petition for relief.

It is our experience that the existing priorities under § 507 of the Code have not seriously impaired the ability of debtors to successfully reorganize in chapter 11 cases.[4] S.548, if enacted, would represent a radical departure from historical bankruptcy policy. Taken as a whole, S.548 creates a *de facto* priority for the benefit of holders of prepetition unsecured employee benefit claims. The creation of such a new class of priority claims, in our opinion, would seriously impair the effective use of chapter 11 and would adversely affect the ability of corporate debtors with significant unfunded retiree medical claims to negotiate out-of-court restructurings of their obligations.

The National Bankruptcy Conference would suggest that Congress consider the creation of a new § 507(a)(5) priority with a defined maximum priority amount per retiree covered by a retiree medical plan. This priority should be designed and the amount thereof determined so as to establish an adequate minimum level of protection for retirees without placing undue hardship on other creditors and without significantly impairing the debtor's ability to reorganize itself and return to financial health. A court could authorize the purchase of insurance or the continuation of payments under a company administered program without having to make a determination in the first hours of the chapter 11 case that the continuation of benefits will result in a higher percentage of recovery to the holders of retiree benefits claims than the recovery to other unsecured creditors. If there is a priority of the type suggested in a reasonable amount, a court could authorize the continuation of benefits to retirees using the same rationale as the courts employ in authorizing post-petition payment of prepetition wage claims up to the $2,000 cap contained in § 507(a)(3).

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[4] The existence of a priority for certain taxes pursuant to 11 U.S.C. § 507(a)(7) and the requirement that a plan of reorganization provide for the payment in full of priority tax claims, with interest, over a six-year period, 11 U.S.C. § 1129(a)(9)(C), makes confirmation of a plan of reorganization impossible in certain cases. Since tax claims were entitled to priority under pre-existing law, this impediment to reorganization is not the creature of the bankruptcy laws.

The ability of the debtor to continue to fund retirement benefits after exhaustion of the specified per retiree cap would be limited in the manner described in the section designated Interim Modification of Retiree Medical Benefits, *infra*.

The caps currently in effect for various priorities in § 507 (other than taxes) range from $900 to $2,000 per creditor or employee. The Conference believes that establishing dollar limits above this range (or granting priorities or administrative expense status without such dollar limitations) should only be done after full consideration of the potential impact of the requirement that such claims be paid upon the reorganization process.[5]

## Representation of Retirees

Section 2(a) of S.548 would create a new § 1113(h) which would make a labor union which is the collective bargaining representative of a unit of employees, the authorized representative of retirees receiving benefits covered by that union's collective bargaining agreement, unless the union elects not to serve as the authorized representative. S.548 would also create a new § 1113(i) pursuant to which the court would be authorized to appoint a committee to represent retirees, if the union elects not to serve as the authorized representative. Such appointment could be made only upon motion of a person receiving retirement benefits under a particular agreement, and after notice and a hearing.

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[5] We have been advised that there are 85,000 LTV retirees. A priority in the amount of $1,000 would create a fund of $85 million as a source for post-petition funding of retiree's medical claims.

Section 2(c) of S.548 would add a new § 1114 entitled Payment of Benefits to Retiree Employees. Pursuant to § 1114(c), upon motion of recipients of retiree benefits not covered by a collective bargaining agreement, the court, after notice and a hearing, is required to appoint a committee of retired employees to serve as the authorized representative of such persons.

NBC Comment:

There is a clear potential conflict between the obligations of a union to existing employees and the rights and claims of retirees. See Century Brass Products, Inc. v. International Union (In re Century Brass Products), 795 F.2d 265 (2d Cir. 1986), cert. denied, 107 S.Ct. 433 (1986). A union should not be the final arbiter of whether a conflict disables the union from properly representing retirees.

NBC Proposal:

The union shall be the authorized representative of retirees covered by a collective bargaining agreement unless the union elects not to serve or, on motion of a party in interest, the court determines that such representation is inappropriate.

If the collective bargaining representative of the unit of employees covered by the collective bargaining agreement covered by this section elects not to serve or is determined by the court to be an inappropriate authorized representative of the holders of retiree benefits claims, the U.S. Trustee shall appoint a committee of retirees to serve as the authorized representative of such claimants. If the U.S. Trustee determines that a committee of retirees cannot adequately represent such claimants with respect to their retiree benefits claims, the U.S. Trustee may request the court to order the appointment of a legal representative to act as the authorized representative of such claimants with respect to their retiree benefits claims.

Interim Modification of Retiree Medical Benefits

Section 2(a) of S.548 would add language to 11 U.S.C. § 1113(e) to state that the prohibition upon unilateral modification of provisions of a collective bargaining agreement includes "any provision relating to benefits for retired employees."[6]

Section 2(c) of S.548 would add a new § 1114(d)(1) which would prohibit the trustee or debtor from modifying retiree benefits unless the circumstances would permit modification under 11 U.S.C. § 1113(e) or the trustee and the authorized representative agreed to the modification. Proposed § 1114(g)(1), however, would permit the court to authorize implementation of interim changes in retiree benefits "if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate."

NBC Proposal

The Conference supports the adoption of proposed § 1114(g)(1). We believe, however, that the standard contained in proposed § 1114(g)(1) should not be the sole basis for interim modification or termination of retiree health benefits. The Conference strenuously opposes the provisions contained in proposed § 1114(d)(2) to the effect that payments made after the filing date and prior to

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6. Section 1113(e) of the Code provides, in part:

> "If during a period when the collective bargaining agreement continues in effect, and if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may authorize the trustee to implement interim changes in the terms, conditions, wages, benefits, or work rules provided by a collective bargaining agreement."

confirmation are entitled to the status of administrative expense claims under § 503 of the Code. Such wholesale expansion of the § 503 priority will undercut the debtor's ability to obtain credit during the pendancy of the chapter 11 case without recourse to § 364.[7] The granting of unlimited priority status to retiree claimants also eliminates any incentive on the part of representatives of retirees to agree to the interim modification of benefit levels.

Retirees should receive their pro-rata share of the debtor's estate to which their prepetition unsecured claims would entitle them. Recognizing, however, the hardship associated with unilateral termination of benefits pending confirmation of a plan of reorganization and final allowance of the retirees' claims, the bankruptcy court should have discretion to permit continuity of payments subject to several conditions. First, payments made to or for the benefit of any retiree group subsequent to the filing date, should be credited against the amount to which such retiree group is entitled as distributions in respect of the priority portion of the retiree benefits claims and thereafter against the non-priority portion of such claims. If it appears to the court that the amount being paid to the retiree group will exceed the amount to which that group would be entitled in respect of their claims, the court may order a reduction or suspension of payments to retirees until a record can be established upon which the court can make a determination that post-petition payments will not exceed the amount to which the retiree group is entitled.

### Proposed Statutory Provision

"On motion of a party in interest, and after a

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7. Section 364 permits the court to approve the extension of post-petition credit with super-priority adminitrative expense claim status.

notice and a hearing, the court shall order the reduction or discontinuance of payment of retirement benefits to any group of retirees if the court finds that, unless benefits are reduced or terminated, the aggregate amount of payments made to such group in respect of retiree benefits claims subsequent to the filing date will exceed the amount to which such group would be entitled in respect of the group's retirement benefits claims. Such determination shall be made on the basis of the facts available to the court at the time of such hearing and may subsequently be modified on motion of a party in interest or by the court sua sponte, if there is a change in the debtor's financial condition."

### Modification of Benefits

Proposed § 1114(d) would provide two methods for the modification of retiree benefits. The trustee and the "authorized representative" can agree to the modification of benefits or, in the alternative, the court on motion of the trustee, and after notice and a hearing, may order modification pursuant to proposed §§ 1114(e), (f), and (g) or pursuant to 11 U.S.C. § 1113(e).

Section 1114(e) would provide that the court "upon motion of the trustee and after notice and a hearing," shall enter an order modifying the benefits payable to retirees whose rights are not covered by a collective bargaining agreement if the court finds that:

> (1) the modifications in the retiree benefits sought by the trustee are necessary to permit the reorganization of the debtor and assure that all creditors, the debtor, and all the affected parties are treated fairly and equitably, and
>
> (2) the balance of the equities clearly favors the entry of an order authorizing the trustee to modify the retiree benefits to the level sought by the trustee . . . .

Section 1114(e) includes an additional caveat that the court may not enter an order providing for a modification in the level of benefits if such modification is "for a level lower than that described in paragraphs (1) and (2)."

Section 1114(f) contains the standard for modification of retiree benefits that are covered by a collective bargaining agreement. Pursuant to this subsection, the court may modify retirement benefits only if the collective bargaining agreement has been rejected under § 1113, and then only if the court finds that:

> (1) it is necessary to permit the reorganization of the debtor and assures that all creditors, the debtor and all of the affected parties are treated fairly and equitably; and
>
> (2) it is clearly favored by the balance of the equities . . . .

Section 1114(f) also contains a caveat that the court cannot order any modification to a level lower than that proposed by the trustee in the trustee's § 1113(b)(1)(A) proposal.

The Conference finds no justification for discriminating between union and non-union retirees with respect to their retirement benefits . Section 1114(f) by creating additional, and in our opinion unnecessary, conditions on the modification of retiree benefits arising under collective bargaining agreements clearly discriminates against non-union retirees.

NBC Proposal

Any permanent modification of the vested rights of retirees constitutes an impairment of the retirees' claims. See 11 U.S.C. § 1124. It is inappropriate to allow the trustee and the "authorized representative" to modify the rights of retirees without their consent. The conditions placed on modifying the claims of retirees in respect of "retiree benefits" are inappropriate. The Code should specifically provide for the permissive separate classification of retiree benefit claims and the group (as opposed to individual) treatment of such claims. Each member of a "retiree benefits class" should be entitled to vote on a one person one vote basis. Modification of the rights of a retiree benefits class pursuant to a plan would require the affirmative vote of a majority of the members of the class voting for or against the plan. Section 1129(a)(7) would have to be amended to provide that the plan could be confirmed if the court determined that the class of retiree claimants (as opposed to individual claimants within the class) would receive distributions in an aggregate amount not less than the amount that they would receive in a chapter 7 case.

These amendments are suggested in light of the fact that actuaries can estimate the present value of medical expenses for a group of retirees on the basis of the terms of their medical plan and the age and residence of the retirees, making appropriate estimation for escalation of medical costs and rate of return on invested capital. Estimating the dollar value of each retiree claim individually would paralyze the bankruptcy courts, delay interminably the debtor's ability to make distributions to retirees or to create an alternate health insurance program and, in all likelihood, deprive retirees of any form of protection in respect of their prepetition unsecured claims.[8] If the goal is the consensual negotiation of alternate medical coverage for retirees consistent with the debtor's ability to pay and the rights of other impaired classes of creditors, specific statutory language permitting group treatment of retiree benefit claims and practical mechanics for obtaining the consent of the holders of such claims, are a necessary part of any coherent legislative package.

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8. In the case of LTV, if a party in interest objected to the individual claims of LTV's 85,000 retirees, and assuming 30 minutes of judicial time to determine the allowed amount of each retiree's claim, the liquidation process would consume 20.43 years of judicial time.

## Classification of Claims

Section 2(d) of S.548 would amend § 1122 by adding a new subsection (c) which would read as follows:

> A plan shall place all claimants for retiree benefits (as such term is defined in § 1114), in a separate class consisting only of such claimants.

## NBC Proposal

The separate classification of retiree benefits claims should be permissive and not mandatory. Certainly there is no justification for the inclusion of all retiree benefits claims in one class since such claimants may derive their benefits under different agreements and the proponent of the plan of reorganization may want to provide different treatment to different retiree groups. For example, the committee representing non-union retirees might negotiate a substitute insurance package funded by distributions to which that group would be entitled and including significant deductibles for treatment not involving hospitalization. A group of union retirees might be offered a different insurance package, administered by the union, and funded by the distributions to which such retirees would be entitled. A third group of retirees represented by a different union could conceivably have a different insurance package funded by distributions to which those union retirees are entitled. Generally accepted rules of classifications would permit separate classification of the three groups to effect the separate treatment of the claims of such groups. The proposed § 1122(c) would introduce inflexibility and thus be counterproductive to the purpose of S.548.

## Confirmation Standards

The class treatment of retiree benefit claims would require certain amendments to § 1123 and § 1129(a) of the Code. First, § 1123 should be amended to provide for group treatment of retiree benefits claims. Second,

§ 1129(a)(7)(A) would have to be amended since a court could not be expected to make a determination that each member of the retiree benefits class would receive under a substitute insurance program at least what the individual retiree claimant would receive in a chapter 7 case. This determination is not possible in large part because the dollar amount of retiree benefit claims can not be determined on a claimant by claimant basis. Third, the amount received by a particular retiree will be a function of that retiree's future medical experience. It should be sufficient that a court makes a determination that the particular class of retiree benefit claimants will receive at least what the class would be entitled to receive in a chapter 7 case.

If a new priority is created with respect to any portion of the claims of retiree benefit claimants, § 1129(a)(9) would have to be amended to address the treatment of the priority portion of retiree benefit claims.

Cram-Down

Section 2(e) of S.548 would amend the cram-down provisions of § 1129(b)(2) to add a new § 1129(b)(2)(C) which would read as follows:

> (C) With respect to a class of claimants for retiree benefits (as such term is defined in section 1114) -
>
> (i) the plan provides that each holder of a claim of such class receives or retains on account of such claim, property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or
>
> (ii) the plan provides that each holder of a claim of such class receive such value as found by the court to represent the minimum reduction in retiree benefits consistent with the ability of the debtor to provide such retiree benefits after confirmation of the plan.

NBC Comment

Proposed subparagraph (C) would require the court to make a determination of the dollar value of each retirees claim which, for reasons discussed above, is impractical in many cases. If the court were able to ascertain the dollar amount of each retiree's claim, subparagraph (C) would require the court to find that the retiree would receive either (i) property of a value, as of the effective date of the plan, equal to the allowed amount of such claim or (ii) "such value" as the court determines represents "the minimum reduction in retiree benefits consistent with the ability of the debtor to provide such retiree benefits after consummation of the plan." It is extremely hard to fathom how the court is supposed to apply the latter standard. If the plan proposes the liquidation of the debtor's assets with payments to be made from a liquidation trust to holders of prepetition unsecured claims (other than retiree benefits claims), no moneys would be available subsequent to confirmation to fund continuing retiree benefits. Thus, any value provided to retiree benefits claimants would constitute a greater value than would otherwise be available post-confirmation. If proposed § 1129(b)(2)(C)(ii) were construed in this manner, satisfying the "cram-down" standard in a liquidating chapter 11 case would be exceedingly simple. On the other end of the spectrum, if the section were to be construed to require post-confirmation cash flow to be first used to fund retiree benefits prior to debt service, recourse to § 1129(b) to obtain confirmation of a plan would be impractical since other prepetition unsecured creditors would not likely accept a plan which effectively subordinated their claims to the claims of retiree claimants.

Section 2(e) should be redrafted to provide for a reasonable standard pursuant to which a plan of reorganization could be confirmed notwithstanding the failure of a class of retiree benefits claimants to accept the plan.

## Effective Date

The National Bankruptcy Conference has consistently opposed retroactive application of bankruptcy legislation and thus opposes the October 2, 1986 effective date.

## RESPONSES OF HERBERT P. MINKEL, JR. TO QUESTIONS OF THE SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE REGARDING S. 548

1. In your testimony, you note that retirees are not members of a collective bargaining agreement (sic) for purposes of section 1113 of the Bankruptcy Code. What evidence can you offer to support the proposition that Congress must not have intended that retirees be covered by section 1113 when the provision was drafted?

ANSWER: It is my view that Congress did not intend for retirees to be covered by section 1113 since Congress would not have protected the right of union retirees to receive benefits post-petition at the expense of non-union retirees. This opinion is based upon the fact that union and non-union retirees are affected equally by termination of medical benefits after the filing of a bankruptcy petition.

There are other more technical reasons why we believe that Congress did not intend for retirees to be covered by section 1113. The section was intended, in part, to reverse that portion of the Bildisco & Bildisco decision in which the Supreme Court held that a trustee or debtor-in-possession could unilaterally terminate a collective bargaining agreement after the filing of a chapter 11 petition without violating the National Labor Relations Act. Thus, a principal purpose of section 1113 was to encourage post-petition negotiations between the trustee or debtor-in-possession and the authorized representative of employees covered by a collective bargaining agreement concerning the terms and conditions of employment. Congress was aware of the fact that modification of the terms and conditions of post-petition employment could be implemented through radification by members of the collective bargaining unit pursuant to procedures sanctioned by the National Labor Relations Act. The members of the collective bargaining unit cannot modify the rights of retirees as part of the post-petition collective bargaining process. The rights of retirees vest at the time of their retirement. If the collective bargaining agreement in existence at the time of retirement makes provisions for life-time medical benefits, the retiree's right to receive such benefits are vested. Any breach of such obligation creates a prepetition unsecured claims. The retirees' rights in respect of such prepetition unsecured claims can only be modified with the consent of the retirees or pursuant to the terms of a plan of reorganization confirmed by the court pursuant to 11 U.S.C. § 1129. We submit that Congress could not have intended that section 1113 be construed to require a debtor to continue to make all payments due to retirees under a collective bargaining agreement in circumstances where the debtor and the authorized representative of current employees cannot consentually modify such obligations. We submit that section 1113 was intended solely to cover the terms and conditions of employment of current employees covered by a collective bargaining agreement with respect to services rendered to the trustee or debtor-in-possession subsequent to the filing date.

2. You point out that additional conditions on the modification of retiree benefits arising under collective bargaining agreements clearly discriminate against non-union retirees. Could you expand on how this discrimination would occur and the probable effect on non-union retirees?

ANSWER: The proposed section 1114 provides that the level of payments in respect of retiree benefits can never be reduced in the case of union retirees below the level of payment contained in the debtor's modification proposal made pursuant to 11 U.S.C. § 1113(b)(1)(A). Thus, the court's discretion in determining the appropriate level of payment is limited in the case of union retirees whereas it is not limited in the case of non-union retirees. Section 1114 also provides that retiree medical benefits may only be modified if the trustee or debtor-in-possession prevails with respect to an application to reject the collective bargaining agreement under 11 U.S.C.§ 1113. Thus, non-union retiree benefits may be modified in cases where the debtor is unable to obtain authority to reject a collective bargaining agreement pursuant to section 1113.

3. Creation of a statutory priority for retiree benefits would have an adverse impact on the ability of Chapter 11 companies to reorganize. Could you detail the possible effect of this bill on the availability of institutional and trade credit for companies seeking to reorganize?

ANSWER: With respect to the availability of institutional credit, a trustee or debtor-in-possession may borrow money in the ordinary course of business after the filing date with a section 507(a)(1) priority. If the trustee or debtor is unable to obtain credit on the basis of the § 507(a)(1) priority, the court may authorize the trustee or debtor to borrow money on the basis of a section 364(c) super-priority. The court may also authorize the grant of collateral to secure the priority or super-priority claim pursuant to section 364(d). Institutional lenders in most cases insist on super-priority secured status under 11 U.S.C. §§ 364(c) and (d). It should be noted, however, that the availability of super-priority status does not necessarily ensure that a trustee or debtor-in-possession will be able to obtain financing. Lenders do not make post-petition loans soley in reliance upon the super-priority status under section 364(c) or collateral granted pursuant to section 364(d). Institutional lenders decline the opportunity to extend post-petition credit if the lenders are concerned about the debtor's ability to repay the post-petition borrowings in the ordinary course. In otherwords, a lender does not want to have to enforce its rights against collateral. It does not want to incur the internal administrative costs associated with liquidating inventory, collecting receivables and disposing of other assets of the debtor. In addition, lenders that are providing "new blood" to the debtor's depleted corpus want to know that the new money is being used by the debtor in its operations as additional working capital. Using this money to fund claims incurred by the debtor prior to the filing date is, from an economic perspective, the same as funding the debtor's post-petition cash losses. In many cases, institutional lenders will not extend post-petition credit to fund significant dollar amounts of retiree benefits. If credit is available, it will cost more since fewer lenders will compete for the opportunity to lend.

With respect to trade credit, an entity providing goods and services to the debtor in the ordinary course of the debtor's business post-petition, is entitled to an administrative expense claim pursuant to section 503 which is entitled to priority under section 507(a)(1). It is not cost effective for most trade creditors to have a lawyer go to court to seek super priority status under section 364. Many credit agreements approved under 11 U.S.C. § 364(c) contain negative covenants against any other creditors having super-priority status. If vendors realize that their priority status is shared by holders of retiree benefit claims in an indeterminate amount, such vendors will protect their self-interest and will decide against extending credit to the trustee or debtor-in-possession. If the trustee or debtor-in-possession cannot obtain credit, the debtor will incur operating problems and the additional cost of financing cash purchases or purchasers supported by letters of credit if L/C support is available.

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## ANSWERS OF HERBERT P. MINKEL, JR. ON BEHALF OF THE NATIONAL BANKRUPTCY CONFERENCE TO QUESTIONS OF THE SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE RE S.548

1. As I read your testimony, it seems to me that you subscribe to the theory that retiree benefits are pre-petition obligations. That being the case, it follows that you would solely on legal grounds, support the decisions of LTV and A.H. Robbins to cut retiree benefits because it was illegal to do otherwise under present law.

   - Is that correct?
   - What advice would you give a company that was in a similar situation, provided the stop-gap legislation was no longer in effect?

ANSWER: It does not follow that I would support the decisions of LTV and A.H. Robbins "solely on legal grounds." It is illegal to pay prepetition claims after the filing date without an order of the bankruptcy court. Pursuant to 11 U.S.C. § 549, the trustee may avoid a transfer of property of the estate which is made after the commencement of the case and is not authorized under title 11 or by the court. I testified during the hearings of the House

Judiciary Committee that LTV should have directed its counsel to seek court authority for continuation of retiree medical benefits at the time of the filing of the LTV chapter 11 petition. Given the potential for disruption of operations (which in fact occurred), we believe that the bankruptcy court would have authorized LTV to continue the retiree medical benefits in effect. I do not have sufficient knowledge of the A.H. Robbins case to comment on the debtor's actions.

2. On behalf of the retirees of Kaiser Steel, Mr. Eckland suggested that this administrative priority be extended to chapter 7 cases and any chapter 11 cases which are later converted to chapter 7.

-Could you please comment on this proposal, and the effect it would have on the bankruptcy process?

ANSWER: We do not believe that the proposed chapter 11 amendment should be carried over into chapter 7 cases. There are serious conceptual problems associated with requiring a chapter 7 trustee to make preferential payments in a chapter 7 case. First, the trustee can be held personally liable if he misallocates property of the debtor. Thus, the trustee cannot make any payments until he is able to determine the allowed amount of claims and the assets available to satisfy claims. If retiree medical claims were entitled to an administrative priority, the trustee in many cases would not be able to finance the costs and expenses of administration if the chapter 7 estate was being used to finance retiree medical expenses. Second, there is no justification in a chapter 7 case for affirmation of a collective bargaining agreement or affirmation of any other prepetition employee benefit plan. The trustee's obligation is to reject all executory contracts if rejection will maximize the percentage recovery on creditors' claims. Third, if the equitable relief embodied in § 1114 has a place in chapter 11 practice, it is based upon the view that the rights of retirees can be accommodated without causing the liquidation of a chapter 11 debtor. The absence of a priority treatment in chapter 7 provides retirees with an incentive to negotiate in good faith to insure that payment of retiree medical benefits will not precipitate a chapter 7 liquidation.

3. You seem certain that passage of this legislation would force more companies into chapter 11 bankruptcies, ~~and~~ force those that are on the borderline into chapter 7 liquidation. It seems to me that this was a concern raised at the time Congress was drafting in the 1984 amendments to the Bankruptcy Code.

   - Has this fear actually come to pass?

ANSWER: I am not aware of any amendment in 1984 which created a substantial realignment of the priority of claims in chapter 11 cases involving industrial debtors. We are sincerely concerned that enactment of S.548 will increase institutional creditors' perceived need for collateral as a condition for going forward with out-of-court restructurings. Those debtors who do not have confidence in their projected cash flows and are concerned about defaulting subsequent to granting collateral to creditors, will resist creditors' demand for full collateral coverage. A special priorities in favor of retiree medical claims will affect the out-of-court negotiating dynamic in industrial cases. Many debtors who would have been able to persuade their creditors to go forward without full collateral coverage, will now be forced to restructure their obligations in chapter 11. If

§ 1114 requires a substantial portion of a debtor's free cash flow to be used to fund retiree medical benefits, the debtor will not be able to generate the net cash flow necessary to create the prospect of significant post-confirmation equity values. In the absence of the prospect of significant equity values, creditors will be less willing to convert debt to equity in a chapter 11 case. Stated differently, creditors will be unwilling to exchange debt claims for equity security if the equity securities are not going to have value. The equity markets value common stock according to projected future cash flow. In order to confirm a chapter 11 plan, the court must find that creditors will receive a higher percentage return on their claims under the chapter 11 plan than in a liquidation. In certain cases, enactment of S.548 in its present form will make it difficult for courts to determine that creditors will do better in chapter 11 than under chapter 7 and this will force debtors into liquidating bankruptcy.

4. In response to this concern, Mr. Humphrey suggests that the legislation provides a number of safety valves for those situations where maintaining retiree benefits will truly cripple the reorganization effort, and points out that retirees recognize that it is in their best interest that the company survive. It seems to me that the Kaiser situation has certainly borne out the later point. Could you comment on this?

ANSWER: My understanding of the Kaiser situation is that Kaiser is not making payments of retiree medical benefits because it does not have cash with which to make these payments. The debtor's failure to make these payments constitutes a violation of existing laws mandating continuity of medical benefits. The Kaiser Steel case appears to confirm the aphorism that "you cannot get blood from a stone." If a debtor is generating excess cash balances by reason of the fact that the debtor is not making payments in respect of prepetition obligations and is operating with a positive cash flow from current operations, payment of retiree health benefits may have no material adverse effect on the debtor's ability to negotiate and obtain confirmation of a plan of reorganization. Section 1114 presents substantial problems when applied to cases in the "middle ground." How does one apportion the debtor's cash flow as between retiree medical benefits, current operations, and creating or maintaining "value" to serve as a means of satisfying prepetition claims. This "value" may be in the form of debt service or net cash flow to support equity value. It should, however, be abundantly clear that a debtor with marginal cash flow after the payment of retiree benefits will not be able to service any significant amount of debt and may not be able to generate net cash flow to support equity value. It is not clear how a court is to balance the needs of the debtor, retirees and creditors. S.548, as drafted, does not provide guidance to the courts as to how to deal with this issue. Therefore, if enacted, it will create more chapter 11 litigation and associated delay and expense.

5. Given the increasing number of bank foreclosures, do you have any information on what effect this legislation would have on banks, the rate of foreclosures, and the willingness to invest in companies?

ANSWER: The above question is not entirely clear. It is a well known fact that the American banking industry has been weakened by problem loans. While a bank may be enjoined by reason of the automatic stay from foreclosing its lien on collateral, the proponent of a plan has to obtain the consent of each class of secured creditors or comply with the "cram-down" standards contained in § 1129(b).

Section 1129(b)(2)(A) requires the court to find that, with respect to a class of secured claims, the plan provides that the secured creditor will receive deferred cash payments totaling the present value of the creditor's allowed secured claim. Diversion of cash flow to service prepetition claims, makes it more difficult for a debtor to satisfy allowed secured claims and thus makes it more difficult to obtain confirmation of a plan of reorganization.

6. One interpretation of the section on interim modifications suggests that the bankruptcy judge would be required to use cash collateral to pay retiree benefits.

   - Can this be done? Is it legal?

ANSWER: Section 363 of the Bankruptcy Code provides that the debtor may not use "cash collateral", as defined in 11 U.S.C. § 363(a), unless the court determines that the secured creditor's interest in the "cash collateral" is "adequately protected." The concept of "adequate protection" is described in § 361 of the Bankruptcy Code and represents Congress' determination as to what is required by way of the minimum protection of a secured creditor's property interest in collateral. It is my view that the use of "cash collateral" to fund retiree medical benefits in circumstances where "adequate protection" is not available would violate the Fifth Amendment of the U.S. Constitution.

7. Am I correct that the benefits that each individual would receive under chapter 11 would have to be determined before a reorganization plan could be confirmed? What is the feasibility of determining the claims of retirees on a case-by-case basis?

ANSWER: Under chapter 11 as presently drafted, 11 U.S.C. § 1129(a)(7) requires the court to determine that each holder of a claim which is part of an impaired class will receive under the plan at least what the holder of the claim would receive in a chapter 7 liquidation. This requires a determination of the dollar amount of each retiree's individual unsecured claim. We have indicated that chapter 11 presently does not contain adequate mechanics for group treatment of these claims. There appears to be a general concensus that the estimation of retiree medical claims on a group basis based upon competent actuarial evidence and the group treatment of such claims by offering substitute insurance coverage is in most circumstances the most sensible course of action. To the extent that S.548 does not include provisions accomodating this end, the National Bankruptcy Conference considers the bill to be deficient.

8. What is the National Bankruptcy Conference's rationale for opposing the retroactive application of this legislation? If the bill is not made retroactive, what could be done in the LTV situation to provide benefits to their retirees?

ANSWER: The National Bankruptcy Conference has always opposed retroactive modification of the bankruptcy laws. The issue is one of fairness. The rules of the game should not be changed after the commencement of a title 11 case. When Congress enacted the Bankruptcy Reform Act in October, 1978, it made the Act applicable to cases filed on or after October 1, 1979. It is our impression that President Reagan shares the Conference's view concerning retroactive modification of the rights of creditors. With respect to the LTV case, we are of the view that this is a non-issue. If LTV threatened to terminate retiree medical benefits, LTV's workers would undoubtedly engage in another "industrial action." The unions in LTV have previously demonstrated that they do not need an Act of Congress to protect retiree medical benefits.

9. Mr. Eklund, representing the retirees of Kaiser Steel, testified that previous discussions with counsel for Kaiser Steel indicate that the company would like to discharge Kaiser's obligation to its retirees by "cashing them out" for approximately 5% of what they are owed. In absolute terms, this seems low. Do you have any information on whether it is low in comparison to other bankruptcy cases you have been involved in? Is there an average?

ANSWER: There is no average. The amount payable to retirees in respect of retiree medical benefits would ordinarily be determined by reference to the value of distributions to be received by other classes of unsecured creditors. Generally, retirees have received a higher percentage recovery in cash which has been used to fund a substitute insurance program, whereas other classes of unsecured creditors have received less cash and a greater percentage of equity securities. The White Motor chapter 11 case illustrates this approach.

10. In the proposed legislation, a new § 1114(h) would be added to the Code which would provide that retiree benefits paid post-petition, but prior to confirmation of a reorganization plan may not be deducted or offset from any amount due the retirees under the reorganization plan, unless otherwise agreed to by the debtor and the authorized representative of the retiree claimants. I am having some difficulty understanding this section.

- Based upon your experience in this area, could you please explain the purpose of this section and the effect it would have if enacted?

ANSWER: By reason of section 1114(h), amounts paid to retirees after the filing date will not be credited against the retirees' ultimate entitlement to distributions under a plan of reorganization. If retirees have aggregate prepetition unsecured claims of $100 million, and if the holder of a prepetition unsecured claim in the amount of $1.00 will be entitled to distributions which have a value of 50¢, under existing law, retirees would be entitled to distributions with a value of not less than $50 million. If $10 million is paid after the filing date and prior to confirmation, under existing law, retirees would receive $40 million under the plan. If there is no credit against distributions, retirees would receive $45 million ($100 - $10 = $90 x .50 = $45 million).If payments made after the filing are not credited against the retirees' ultimate right to distributions in the chapter 11 case, the retiree representatives will have no incentive to agree to interim modification of retiree medical benefits so as to adjust the level of benefits to the debtors' ability to pay. Retiree representatives will insist on full benefits during the reorganization case unless the funding of benefits will force the debtor to liquidate. On the other hand, if benefits are credited against the ultimate right to receive distributions, representatives will have an economic incentive to negotiate modifications in order to preserve the size of the fund which will be used to pay retiree medical benefits after confirmation of a plan of reorganization. Section 1114(h) also acts as an economic incentive for retiree representatives to delay the chapter 11 process since payments received subsequent to the filing date and prior to confirmation will not be credited against the retiree's right to distributions. The National Bankruptcy Conference believes that this section represents an unnecessary and unjustifiable enhancement of the rights of retirees; that the provision works against consentual modification of retiree benefits by reason of the debtor's impaired financial condition; and that section 1114(h) is not necessary to ensure continuity of benefits after the filing and the equitable treatment of retiree health claims pursuant to a plan of reorganization.

11. NBC suggests that Congress create a new § 507(a)(5) priority with a defined maximum priority amount per retiree covered by a retiree medical plan.

- How would you go about settling that amount given that the situation will vary dramatically from retiree to retiree?

ANSWER: The amount provided for in the proposed new § 507(a)(5) priority would not be determinative of the dollar amount which a particular retiree would receive for medical claims arising after the filing date. The new priority would define the dollar amount of a fund which would be available to support post-petition payments. The size of that fund would be equal to the number of retirees multiplied by the dollar amount of the priority. If this fund was exhausted during the chapter 11 case, the court could authorize additional payments to be made in respect of retiree medical benefits but these payment would be credited against the distributions to which the retiree benefits claimants, as a group, would be entitled under the plan of reorganization.

12. As you know, the proposed legislation would elevate the status of retiree benefits to administrative expenses during the pendency of the petition.

- This being the case, are there other rights which should receive consideration for similar treatment?

ANSWER: In our view, the issue is not whether other rights should also be afforded administrative expense priority. We believe that the administrative expense priority should be limited to those entities which provide credit, goods or services to the trustee or debtor-in-possession during the chapter 11 case. Creating additional categories of administrative expenses, dilutes the value of the priority and thereby makes it more difficult for the trustee or debtor-in-possession to obtain credit in the ordinary course during the chapter 11 case. This will thwart the statutory purpose of chapter 11.

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## RESPONSES OF HERBERT P. MINKEL, JR. TO QUESTIONS OF THE SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE REGARDING S. 548

1. Under current bankruptcy law, various parties may wish to extend credit to a debtor-in-possession, after the debtor company files its petition. The code contains some incentives, such as the "administrative priority" under section 503, so that lenders and other creditors can help the business get back on its feet. Would you agree that one of the needs of any debtor in chapter 11 is access to new credit?

ANSWER: Yes.

2. If, under S. 548, we now add an additional level of claimants who will get administrative priority treatment, what does this do to the order of payment to those who provide new credit?

ANSWER: Creating an additional level of claimants entitled to priority under 11 U.S.C. § 507(a)(1) dilutes the benefits of such priority. The administrative priority was intended to provide assurance to entities providing goods and services to the trustee or debtor-in-possession that they will receive payment prior to prepetition creditors.

3. Accordingly, does adding this class of claimant discourage the continued flow of credit to the debtor, particularly when the debtor may need it most?

ANSWER: Yes.

4. Please explain section 1114(h). Does this mean that the debtor cannot deduct post-petition payments from what the court ultimately agrees on in terms of a modification of the benefits? What is your opinion of such a provision?

ANSWER: By reason of section 1114(h), amounts paid to retirees after the filing date will not be credited against the retirees' ultimate entitlement to distributions under a plan of reorganization. If retirees have aggregate prepetition unsecured claims of $100 million, and if the holder of a pre-petition unsecured claim in the amount of $1.00 will be entitled to distributions which have a value of 50¢, under existing law, retirees would be entitled to distributions with a value of not less than $50 million. If $10 million is paid after the filing date and prior to confirmation, under existing law, retirees would receive $40 million under the plan. If there is no credit against distributions, retirees would receive $45 million ($100 - $10 = $90 x .50 = $45 million).

If payments made after the filing are not credited against the retirees' ultimate right to distributions in the chapter 11 case, the retiree representatives will have no incentive to agree to interim modification of retiree medical benefits so as to adjust the level of benefits to the debtors' ability to pay. Retiree representatives will insist on full benefits during the reorganization case unless the funding of benefits will force the debtor to liquidate. On the other hand, if benefits are credited against the ultimate right to receive distributions, representatives will have an economic incentive to negotiate modifications in order to preserve the size of the fund which will be used to pay retiree medical benefits after confirmation of a plan of reorganization. Section 1114(h) also acts as an economic incentive for retiree representatives to delay the chapter 11 process since payments received subsequent to the filing date and prior to confirmation will not be credited against the retiree's right to distributions. The National Bankruptcy Conference believes that this section represents an unnecessary and unjustifiable enhancement of the rights of retirees; that the provision works against consentual modification of retiree benefits by reason of the debtor's impaired financial condition; and that section 1114(h) is not necessary to ensure continuity of benefits after the filing and the equitable treatment of retiree health claims pursuant to a plan of reorganization.

5. With respect to proposed sections 1113(h) and (i), these sections provide that the union can decline to serve as the authorized representative. Under what circumstances might the union decline?

ANSWER: In any case where a union represents retirees and current employees, there is a theoretical conflict of interest. The retirees are interested in maximizing the percentage recoverable on their claims. The current employees are interested in preserving their jobs and minimizing any reduction in the level of salaries and benefits. In some cases, there is a concentration of employment and generations of families may have been employed by a debtor. In those cases, social and family bonds may cause employees to make concessions in favor of retirees. It is not possible, however, to generalize concerning the attitude of current employees with respect to retiree benefits. A debtor may have closed an old plant and opened a new plant in a different geographical area. Current employees may have no social or familial ties to retirees and may be less sympathetic to the economic hardship which bankruptcy may visit upon retirees. In many unions, retirees are not members of the collective bargaining unit, and may not vote in union elections. In such situations, the union leadership may well recognize that its responsibility is to maximize the level of compensation and benefits payable to current employees. In such circumstances, the union representatives may determine that they cannot properly represent retirees who were represented by the union.

6. What if the union wants to represent retirees but some of them believe the union won't do a good job for them? Can some retirees "opt out" of union representation?

ANSWER: There is no provision in S. 548 for an "opt-out" of retirees who do not wish to be represented by the union in negotiations concerning the modification of their retiree benefits. The National Bankruptcy Conference has suggested that any retiree should have the opportunity to request the court to consider whether a particular union is an appropriate representative of a group of retirees in the particular circumstances of a chapter 11 case. If a motion is made for the appointment of a committee to act on behalf of a group of retirees, any party in interest should have standing to be heard on such motion. The National Bankruptcy Conference has also suggested that the court should have the power to appoint a legal representative to represent a group of retirees if the court is satisfied that the retirees cannot be effectively represented by the union and cannot effectively represent themselves through a committee.

7. The union's primary responsibility is to current employees. When "push comes to shove", how can there not be a conflict of interest where the representative of the retirees also represents current employees? For example, current employees may be out of a job due to a chapter 7 liquidation -- precipitated by the payment of these benefits.

ANSWER: See the Answer to question 5.

Senator HEFLIN. Thank you, sir.

Mr. King?

Mr. KING. Thank you, Senator. I do not have a statement. Mr. Minkel has prepared the written statement and has given the oral statement, so I will try and help with any questions that you may have.

Senator HEFLIN. Aside from making the retiree benefits an administrative expense, is there any way to insure that the retirees receive payment of that benefit? What does the creation of this administrative priority do to the dynamics of out of court workouts in chapter 11 bankruptcy?

Mr. KING. Well, one of the things it seems to us that would certainly occur by making this an administrative expense is, it would be extremely difficult if not impossible for a chapter 11 debtor to get any financing elsewhere. And if the chapter 11 debtor cannot get the financing from an institutional lender to continue operations in chapter 11, then, as Mr. Minkel was pointing out, there is a greater likelihood of companies going into liquidation. That is No. 1.

Second, with this kind of a threat hanging over the possibility of a chapter 11 filing, I think that the creditors generally would be less likely to engage in an out of court workout, in case that were to fail they would not be willing to extend credit during that period of time before a petition is filed.

Senator HEFLIN. Do you have anything to say, Mr. Minkel?

Mr. MINKEL. Out of court, Senator, what the institutional creditor is looking for is security, and what the board of directors of a debtor company is trying to do is to restructure and put the company at the least risk of liquidation, and therefore the dynamic is not to give collateral to institutions unless you are sure that the company can make it out of court. That it can make its business plan.

By creating large priorities that come out ahead of unsecured creditors, what you have done is you have increased the perceived need of institutions to have collateral and that will cause directors to say we are better off in chapter 11.

Chrysler would not have succeeded in restructuring its institutional debt and would not have survived without trade credit. Trade credit is unsecured credit and the trade will not extend credit outside of bankruptcy in circumstances where there is a risk that all the money is going to go to retirees after bankruptcy.

Mr. KING. Senator, if I might add one further thing. It is a more general comment but I think that it may be worth saying or even repeating if it has been said before. This committee is looking at one particular problem. Part of the solution that is contained in the bill is to create an administrative priority.

There are other problems that are being looked at by other people, by other agencies of the government. The ERISA statute itself has been mentioned. PBGC has been mentioned. One of the things that PBGC has been asking for over the last couple of years and will come to this committee, I am sure, asking again is for a superpriority for a PBGC claim, for it to have a secured claim, if not a superpriority claim, or to have both, so it would get paid ahead of everybody and anybody.

In past years since 1978, when the Bankruptcy Code became effective, there have been similar situations of landlords coming in for particular priorities and fishermen coming in for particular priorities. Each of these has been treated on a piecemeal basis. The net result of all of this is going to make chapter 11 basically a nonexistent process, and as a result there will be many fewer companies that will just go out of business, period, to the detriment of everyone.

So if this is a problem, it seems to me, and I would say also to the National Bankruptcy Conference, that it is something that should be looked at as a whole and not on a piecemeal basis.

Senator HEFLIN. On behalf of the retirees of Kaiser Steel, Mr. Eklund suggested that this administrative priority be extended to chapter 7 cases and any chapter 11 cases which are later converted to chapter 7 cases. Could you please comment on this proposal and the effect that it would have on the bankruptcy process?

Mr. MINKEL. Well, the purpose of section 1113, the section on collective bargaining, was to have good-faith bargaining after the filing, to not have the employer terminate benefits immediately after the filing, to negotiate in good faith to try to resolve collective bargaining issues consensually, and Congress felt that section 113 harmonized the policies of the Bankruptcy Code and the policies of the National Labor Relations Act.

In a chapter 7 case, a trustee does not have discretion to enter into the modification of such agreements. Chapter 7 involves determining who has allowed claims and, when those claims are determined, the trustee liquidates assets and distributes the proceeds of liquidations. The process of figuring out what the claims are and whether there are any assets to be distributed, in many chapter 7 cases, takes years. A trustee can be personally surcharged if he makes a payment which is not supported by the statute. The trustee is not going to be able to make any payments on the day after bankruptcy to retirees in a chapter 7. Anybody who has ever had the opportunity to be a chapter 7 trustee, realizing that he is personally liable and is going to be very circumspect about how to deal with the problem. While preserving coverage in chapter 7 sounds good, in reality, it is not possible, Senator.

Mr. KING. It raises a point that I had made before, too, that if that priority continues over from a chapter 11 case after it is converted into a chapter 7 case, it would make it more difficult to get financing by any lender in that chapter 11 case because that priority would not be carried over into a subsequent chapter 7 case, resulting in either not getting any credit to operate in the chapter 11 or in that lender insisting on taking collateral which would probably use up all of the available free assets, so the administrative priority is not going to be worth anything if all of the assets are collateralized.

Senator **Heflin**. There is a vote on the Senator floor and I have 1½ minutes to get there. Senator Metzenbaum must have been held up; so if you will wait until he comes, we will have a little recess, and he can reconvene the hearing.

[Short recess.]

Senator **Metzenbaum**. The subcommittee will come to order.

It takes a little time to get over to the floor of the Senate and back.

Mr. Minkel, you are here on behalf of the National Bankruptcy Conference, and you, Mr. King, are also here on the same basis. Let me, just to be certain that, do you have any clients that have an interest in the LTV matter, the A. H. Robins matter, Kaiser Steel or any of those bankruptcy proceedings?

Mr. **Minkel**. I do not have any clients that have any interest in any of the three cases, with the exception of one relatively small trade creditor who delivered goods to LTV within 10 days of the filing based on promises that he was to be paid and who is asserting a reclamation claim.

Mr. **King**. Senator, I am counsel to a law firm of Wachtell, Lipton, Rusen & Katz, and that firm represents the creditors' committee in the *Robins* case, and I understand that it just took on representation as cocounsel to the creditors' committee in LTV. I think that is within the last month. I say I think that because I have been away from the country for the last 4 months myself.

Mr. Minkel. As you may be aware, Senator, Professor King has been teaching this semester at Hebrew University in Jerusalem and he came back yesterday in order to appear before you. He only discovered accidentally before he came to Washington that his firm is now involved in that capacity in LTV.

Senator **Metzenbaum**. All right. I just sort of thought we ought to have it on the record.

Your testimony directly contradicts the testimony this committee received from Professor Vern Countryman last year respecting current law protections for collective bargaining agreements. He testified that section 1113 protects all benefits in a collective bargaining agreement, including those for retirees, and the House under the leadership of Chairman Rodino last year passed what they termed a clarification of current law that states retiree benefits are covered by section 1113. And the second circuit, in *Century Brass,* last July indicated that retiree benefits are covered by section 1113.

Section 1113 itself states that it covers "all provisions of a collective bargaining agreement," and there are no exceptions. I then have to ask you on what basis do you reach the conclusion that Congress did not intend for section 1113 to cover retiree benefits?

Mr. **Minkel**. Senator, first of all, I do not think the court in *Century Brass* held what you just said it held. What it said was that retirement benefits are a mandatory subject to collective bargaining, and the rationale was that there was potential conflict between the rank and file union members and the retirees and to the extent that a retirement benefit would bleed the company and cause——

Senator **Metzenbaum**. Do not speak so fast. Slow down just a little bit.

Mr. **Minkel**. All right. To the extent that the retiree benefits could in theory bleed the company and cause the debtor to not be viable and cost the rank and file union members their jobs, the second circuit felt that it was a proper subject of bargaining but it did not say it was covered by section 1113 in the sense that the company would have to continue to make the payments postfiling.

The distinction, Senator, is that all claims which arise prepetition are prepetition claims which cannot be paid after the filing without a court order. Now, that rule also covers claims that arise under collective bargaining agreements.

Someone who worked under a collective bargaining agreement prior to the filing and was not paid his salary for the 2 weeks prior to the filing was a prepetition claim. It happens to be covered by a priority in section 507, and very often a court, because there is a $2,000 priority per employee, allows the wage claim to be paid. But it takes a court order to authorize payment.

Section 1113 was your response, Congress' response to *Bildisco & Bildisco,* where the Supreme Court said that immediately after a filing a debtor could unilaterally terminate a collective bargaining agreement. Congress said that is not right and passed a law which said there should be negotiations after the filing before the terms and conditions of employment of union members are altered. A debtor should not be able to do it unilaterally.

To the extent that the current employees consent to the changes in their terms of employment, they have an opportunity during the chapter 11 case to ratify pursuant to a ratification vote any amendment to their contract.

Retirees cannot do that. Retirees are not members of the collective bargaining unit and the union, if it agreed to a reduction in the retirees' vested rights, could not make that binding on the retirees because the retirees have under the bankruptcy laws a right to vote on any modification, any impairment of their claims.

There should be legislation in this area. In a case in your State, the *White Motor* case, even though White Motor did not survive, retiree medical benefits for the union retirees were preserved by the purchase of a medical policy. The policy had fewer benefits than existed before, but there was continuity of coverage. It worked by reason of the good faith of the company, the good faith of the creditors' committee and the good faith of the union that was representing the retirees in that case.

That plan was confirmed notwithstanding the fact that the law did not support the group treatment of retiree claims but it was the only way to get them what they needed, namely, some kind of blanket substitute protection.

To the extent this bill addresses that problem, it is commendable.

Senator **Metzenbaum**. Mr. Minkel, you take the position that *Century Brass* does not cover the issue with respect to the retirees, and yet *Century Brass* dealt with the question of who represents the retirees under section 1113. If section 1113 does not cover retiree benefits as it specifically says it does, then why would the court reach the issue of who represents the retirees under section 1113?

Mr. MINKEL. I think a fair reading of this issue is the court was dealing with——

Senator METZENBAUM. Pardon?

Mr. MINKEL. I think a fair reading of the decision is that the court was dealing with one issue and that was whether there was a potential conflict of interest. The court said there was a potential conflict of interest and that the union appropriately was standing down. That was what the second circuit was asked to review and that is what they reviewed.

Senator METZENBAUM. But they would only be dealing with that issue of who represents the retirees if the retirees had a claim, a judiciable claim in that case, and that is the point that I am making.

Mr. MINKEL. I think the retirees have claims under the agreement. It is just that the claims are not executory. The concept of an executory contract, Professor Countryman's definition of an executory contract is a contract in which there are substantial duties to be performed by both parties.

Retirees have no duties to perform unlike employees. Retirees have vested rights which are vested and cannot be changed pursuant to collective bargaining. They are vested as defined by the Supreme Court of the United States in *Pittsburgh Plate Glass*. Justice Brennan said they are vested prepetition claims, they cannot be modified pursuant to collective bargaining negotiations.

Now, I cannot imagine that you intended, Senator, to set up a system for negotiation for modification of something that cannot be negotiated in the collective bargaining process.

Senator METZENBAUM. Let me talk about the question of retirees. You are urging that they be set back in position and yet, during the first 3 months of LTV's bankruptcy, the court has approved payment of nearly $3 million in legal fees. I do not know whether your firm is one of them. I gather that it is not. But Davis Polk, more than $1.5 million; Jones, Greg, Quiegan & Grace, $35,000; LeBoeuf Lamb, $235,000; Levin Weinthraub, $432,000; McKenna Connor, $15,000; Rein Harrell, $15,000, Squire, Sanders & Dempsey, $64,000; Strook, Strook & Levan, $475,000; Verner Liipfert, Bernhard, McPherson & Hand, $103,000—I think I skipped one—Bauman & Associates, $17,000, a total of $2,989,000 in a 3-month period.

Vern Countryman testified last year that legal fees could easily amount to $18 million when the bankruptcy case is over. I think these figures show that his estimate is actually low.

Mr. Minkel and Mr. King, how much do you think the legal fees in the LTV case will finally run?

Mr. KING. I would not hazard a guess on that.

Senator METZENBAUM. How come you can guess about everything else but you cannot guess on that? [Laughter.]

Mr. KING. Senator, I try not to guess.

Senator METZENBAUM. But you are experienced, you are an expert in this field.

Mr. KING. I am not experienced in terms of going into court and asking for a fee, let us put it that way; and I really do not keep track of bankruptcy fees, because one of my problems back in the drafting of the 1978 code is that as long as they are not providing for law professors to get paid out of bankrupt estates I was not going to concern myself with the fees that get paid.

Senator METZENBAUM. But if you come in as a consultant to the law firm or as an associate of the law firm, then you do get paid?

Mr. KING. I get paid by the law firm, that is correct.

Senator METZENBAUM. And the hours that you put into this case, the firm would be billing for?

Mr. KING. That is correct.

Senator METZENBAUM. At what rate?

Mr. KING. At the rate of $350 an hour, I believe. I am trying to think whether it just went up. I think it is $350.

Senator METZENBAUM. And, Mr. Minkel, what is your estimate as to what the fees will be in the LTV case?

Mr. MINKEL. The reason it is impossible to estimate, Senator, is that legal fees are a function of time. The longer the case takes, the larger the legal fees are. The more litigation there is in the case, the larger the fees will be.

One of the things that was a breakthrough in Congress' construction of chapter 11 during the period from 1973, when the Commission on Bankruptcy Law rendered its report to 1978, when Congress passed the Bankruptcy Reform Act, was the streamlining and simplification of chapter 11 practice so as to encourage out-of-court workouts; but, second, to make it quicker to get a company through chapter 11, and I think that has generally worked. It has taken less time to reorganize under chapter 11 than it took under chapter X. This saves money on legal fees.

Senator METZENBAUM. Let me ask you again, what do you think it will cost, the legal fees?

Mr. MINKEL. I think you can take, if they are running at——

Senator METZENBAUM. $3 million for——

Mr. MINKEL. For 8 months?

Senator METZENBAUM. For 3 months.

Mr. MINKEL. For 3 months?

Senator METZENBAUM. July 17 to October 31, a little over 3 months.

Mr. MINKEL. Those are the first 3 months of the case and generally the burn rate is higher, but if they are $5 to $10 million, I would think that it would take at least 2 years to get that company through. Now, that is assuming that people can get together and negotiate in a sensible manner and come up with a consensual plan of reorganization. There are cases that are consensual and they move through the courts quickly and there are situations where chapter 11 is a battleground and the *Manville* case was like that. Where people did not want to negotiate with one another, and the burn rate was much higher.

Senator METZENBAUM. What do bankruptcy fees run on the average, would you say, per hour, about $350, $400?

Mr. MINKEL. No, $350—Professor King, being the preeminent expert in the field, commands a higher premium I think than most practitioners. It depends on where you are in the country but it probably runs from $40 an hour in certain parts of the country for associates up to in between $200 and $300 an hour in major cities for people that are considered to be the top members of the bar.

Senator METZENBAUM. $400? According to Countryman, he indicated that he thought that the fees were running $400 an hour.

Mr. MINKEL. I do not know of anyone in New York who charges $400 an hour.

Mr. KING. Maybe Vern Countryman charges $400 an hour.

Senator METZENBAUM. I do not know what Vern Countryman charges.

Mr. KING. Neither do I.

Senator METZENBAUM. But he is not in this case.

Mr. KING. I ought to add——

Mr. MINKEL. I think he is in many of these cases as an advisor to various unions.

Senator METZENBAUM. I do not have any question about that, but the point that concerns me is that we are talking about $100 million to take care of the retirees for 1 year and we are looking at fees that, if the projections come out, are about $12 to $15 million in 1 year just for legal fees, as against that $100 million. If you are a retiree you have to be pretty upset about that.

Mr. Minkel. I think that if you have a case that is tied up in court because of litigation among parties, recognizing that interest does not accrue on claims of insolvent estates after the filing unless they are secured, and that there is a loss in present value with every day that a case gets delayed, I think every creditor in a chapter 11 can be legitimately upset if people are not getting together and trying to negotiate and trying to give something up and trying to work through problems to get a live debtor through the reorganization process. All we have said in our testimony is that retirees should be part of that process and not protected as a special group because there are retirees who are bond holders and they survive on the interest that accrues on those bonds; when this debtor goes into bankruptcy they do not get any more interest. And there are mom and pop vendors who call me up after a filing and say, "Mr. Minkel, I have to get paid or I'm going to lose my business," and there are hundreds and hundreds of banks that have gone out of business in the last year, and if they do not extend credit, Congress gets upset and when they do extend credit and go down the tubes, Congress has to bail out Federal agencies that insure deposits, and you get upset.

Bankruptcy is a nasty business. It is a better business in this country than the alternatives in Europe and in other places, where they only liquidate companies. There are so many examples in your State where companies have survived chapter 11 or have avoided chapter 11 because people have made concessions out of court rather than go through chapter 11. If the creditors could have just liquidated the company, they would have done that.

Senator METZENBAUM. I have no further questions. Thank you.

Our next witness is Bruce Hendry, chairman of the board and chief executive officer of Kaiser Steel.

Mr. Hendry, we are happy to have you with us, sir.

## STATEMENT OF BRUCE E. HENDRY, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, KAISER STEEL CORP., ACCOMPANIED BY JOHN CONNALLY, GENERAL CORPORATE COUNSEL; AND CRAIG CHRISTENSON, SPECIAL BANKRUPTCY COUNSEL

Mr. **Hendry**. Thank you, Mr. Metzenbaum.

As you pointed out, I am Bruce Hendry, chairman of the board and CEO of Kaiser Steel. Kaiser Steel being the former steel maker now in chapter 11.

On my left is John Connally, from the law firm of Lindquist & Vennum, Lindquist & Vennum being the general corporate counsel for Kaiser Steel; on my right is Craig Christenson, from the law firm of Sherman & Howard, Sherman & Howard being the special bankruptcy counsel for Kaiser Steel.

Senator **Metzenbaum**. I am not going to ask them if they get $400 an hour in fees. [Laughter.]

Mr. **Hendry**. I believe their fees are somewhat less.

I have heard the testimony this morning and I have to tell you that I believe that I am personally, and I think the people at Kaiser Steel management are probably, in sympathy with what your law is trying to do and that is to create fairness for the retirees.

What concerns me, however, about the testimony and about the law itself is simply this, that Kaiser Steel truly is different than LTV and the other steel companies. In fact, we do not even make steel any more. If this law goes into effect without modification, it is really going to——

[Recorded message played over P.A. system]

Senator **Metzenbaum**. That is good news. That was a report saying no more rollcalls today. I thought I was going to have to cut you off and go for a rollcall, but proceed.

Mr. **Hendry**. When you said it was good news, I thought maybe that you were going to amend your law. [Laughter.]

Senator **Metzenbaum**. You never can tell.

Mr. **Hendry**. What I am afraid will happen, Senator, is simply this, that in everyone's effort to accomplish what is a social good using the bankruptcy laws to do it, that you are going to throw out the baby with the bath water. I have got to tell you that Kaiser Steel is the baby.

If you pass the law unmodified, we are done, we are probably going to go into a chapter 7, and I think even you pointed out in the testimony when you read the article from the Plain Dealer that LTV may in face survive and be a profitable company. This is the best outcome for chapter 11, because by doing that you increase the value for all the creditors to the retirees. In our case, retirees make up the bulk of the creditors and the retirees, as Mr. Eklund pointed out to you, are in fact on the creditors committee.

We filed chapter 11 not out of any business strategy. We filed chapter 11 because we did not have any money. I am not sure you know the background of Kaiser Steel, so just let me tell you the background of how I got in, it was through a proxy fight.

I had observed that former management were doing things that I thought were not in the best interest of bond holders particularly, because I was one—preferred stock is the actual instrument—and other creditors, and a proxy fight ensued which I eventually won. My first day on the job was January 7.

On that day I was called into the conference room and I was told by the people there, "Mr. Hendry, we don't have enough money to get past 5 o'clock this afternoon. What are we going to do?" Well, the only way we got past 5 o'clock that afternoon was to have someone prepay a bill at a very substantial discount.

The next week, basically the same situation occurred and it was a choice between making payroll, literally keeping the lights on because we were in danger and notification that the lights and telephone would be turned off, and this was the situation that Kaiser Steel found itself in.

Senator METZENBAUM. What were you at that time, you were the chairman at that point?

Mr. HENDRY. Yes, as a result of the proxy fight, on January 7 of this year I was installed as chairman of the board and chief executive officer.

Senator METZENBAUM. Have you concluded?

Mr. HENRY. No, no. I just want to point out that chapter 11, I think, is therefore with a purpose and a good purpose. Some of the prior speakers pointed out that chapter 11 has been used for other purposes in certain cases, business strategies. This business strategy is simply to survive and we think that—I cannot say that we are going to survive. I can tell you——

Senator METZENBAUM. You are not operating now?

Mr. HENDRY. We are not operating a steel mill. We do have some coal operations going. Those coal operations are currently losing money. We are trying to get them to break even or even positive cash flow. That has not happened yet.

I do want to point this out to you, Senator, that Kaiser Steel, and I only speak for Kaiser Steel, but Kaiser Steel is making a good-faith effort with their retirees. The retirees are on our creditors committee. We are negotiating with them at this very moment to work out some interim arrangement to pay what we call the Metzenbaum requirement.

Senator METZENBAUM. Are some of the employees now receiving medical benefits?

Mr. HENDRY. Well, there are approximately 7,000 retirees that we are obligated to.

Senator METZENBAUM. But I said, are they receiving benefits?

Mr. HENDRY. No, they are not receiving benefits.

Senator METZENBAUM. What does it mean, the present employees of Kaiser Steel Corp. and Kaiser Coal Corp. have been afforded reduced medical and disability coverage? What does that mean.

Mr. HENDRY. Well, in order to keep our employees, we had to provide some coverage or they would walk off the job, and that is what that means.

Senator METZENBAUM. But they are not working, the steel plant is shut down.

Mr. HENDRY. The steel plant is shut down but our coal operations are still working. We still have some 1,000 employees.

Senator METZENBAUM. I see. Some retirees took lump sum settlements. Were all of them given that same opportunity?

Mr. HENDRY. That was before my time, but it is my understanding that they were, yes.

Senator METZENBAUM. I think I have no further questions.

Mr. HENDRY. I am sorry, are there further questions?

Senator HEFLIN. Do you consider that this reorganization will in effect dilute the value of the shares of stock that are involved in your company?

Mr. HENDRY. Well, the common shares are held by a single entity called the Perma Group, and it is my belief that they will be totally and completely washed out.

Senator HEFLIN. I believe that is all.

Senator METZENBAUM. I have a couple more.

Your predecessor was receiving $2.3 million a year, Mr. Reil?

Mr. HENDRY. Yes, that is correct.

Senator METZENBAUM. And until what point did that continue on, and did he get any bonus or retirement arrangement when he left?

Mr. HENDRY. No, he was essentially fired when I came on board. That is what the proxy fight was all about. As a matter of fact, we have instituted lawsuits against Mr. Reil to recover some of these funds which we think were improperly taken.

Senator METZENBAUM. The prepared testimony submitted by the Retired Creditors Subcommittee indicates that a proposed plan of reorganization is being fashioned by Kaiser. The testimony indicates that the retirees may only receive 5 cents for every dollar promised. Do you think that that is about what the retirees may expect to receive?

Mr. HENDRY. I cannot imagine where that figure came from. It certainly never came from my lips.

Senator METZENBAUM. I think it was the retirees unsecured creditors, in their testimony I think they used that figure.

Mr. HENDRY. Yes, I read that but I cannot imagine where that came from. I can tell you this: If the bill that is proposed here passes unamended, that this company will probably go into a chapter 7, and in that particular case a 5-percent settlement is not impossible, but again I have not really addressed that.

Senator METZENBAUM. Actually, the company is now paying almost $2 million a year in salaries, half a million dollars in benefits, half a million dollars for phone and utilities, $300,000 for travel. Is that pretty accurate?

Mr. HENDRY. When you threw all those figures at me fairly quickly, we have dramatically cut all the expenses in just our 3 months of operation. Where there were some—do not hold me to this figure, but I think there was something like $14 million worth of salaries paid to executives that were paid over $100,000. There are now only $550,000 per year and that is among three executives, down from very many from the prior——

Senator METZENBAUM. Down from $240,000?

Mr. HENDRY. That is right.

Senator METZENBAUM. Tell me this: You say that if this bill passes you may be forced into chapter 7.

Mr. HENDRY. That is correct.

Senator METZENBAUM. When do you think you can put your reorganization together, how soon?

Mr. **Hendry**. Again, it depends on the parties. Currently, I feel we have good relationships with all the creditors and we are hopeful that we can do something very quickly.

Senator **Metzenbaum**. Well, I would say that if you do something very quickly you will not have to worry about this bill because we are not going to pass it this week. [Laughter.]

But I think you have a little lag time and I would just urge you to go ahead and get your reorganization done. We wish you well. We would like to see you back in operation, but I do not think that the solution is to change our bill. I think the solution is for you to get your reorganization done before we pass our legislation. It is not applicable now.

Mr. **Hendry**. That is good advice and we certainly will work at it.

Senator **Metzenbaum**. All right. Thank you.

Mr. **Hendry**. Thank you.

Senator **Metzenbaum**. Thank you, Mr. Chairman.

[The prepared statement of Mr. Hendry follows:]

# TESTIMONY OF BRUCE E. HENDRY PRESENTING THE POSITION OF KAISER STEEL CORPORATION ON SENATE BILL 548

Mr. Chairman and Members of the Committee. My name is Bruce Hendry. I am Chairman of the Board of Directors and Chief Executive Officer of Kaiser Steel Corporation.

As you know, Kaiser Steel Corporation filed for protection under Chapter 11 of the United States Bankruptcy Code on February 11, 1987. I want to give you a brief history of Kaiser Steel Corporation in order that you might understand the events which led to the filing of its Petition for Relief. Kaiser Steel Corporation at one time was one of the families of companies that came under the Kaiser umbrella. These included Kaiser Aluminum, Kaiser Cement and Kaiser Permanette, a health care organization which were held by Kaiser Industries, Inc., a publicly traded holding company. Approximately 10 years ago Kaiser Industries, Inc. was dissolved. Kaiser Steel's primary business was the production, manufacturing and marketing of steel products. However, Kaiser Steel operated a number of other businesses which were at one time a subsidiary to the steel-producing business. These included coal mining, iron ore mining, limestone mining and steel fabrication facilities located in New Mexico, Utah and California.

As the steel industry became more competitive in a worldwide market in the late 1970's and early 1980's, it became apparent that Kaiser Steel would be unable to compete with the foreign producers. Consequently, its principal steel production facility was sold in 1984 to a consortium of buyers led by Brazilian and Japanese groups. With the closing of the steel mill at the time of that sale, Kaiser Steel effectively was no longer in the steel production business. After the closing of that sale in 1984, Kaiser Steel no longer had any active employees represented by the United Steel Workers Union except a small force at one of the steel fabricating products facility.

Prior to the sale of the steel production facilities, Kaiser Steel had been providing generous medical and pension benefits for its hourly employees and its salaried employees. Unfortunately, the cost of those plans were either never accurately recognized or adequately funded. This inability to totally fund those benefits was recognized shortly after the sale of the steel production facility, and Kaiser Steel Corporation entered into separate contracts with approximately 5,600 of its retired workers providing those workers with medical and health benefits that were reduced from that which had been provided to them by the expired Collective Bargaining Agreement. In addition to those individual contracts, a number of workers received a cash settlement from the Company in satisfaction of all future claims that they may have had for health benefits. These settlements ranged in the area of $6,000 to $18,000 per worker depending on the former employee's age and number of dependents.

Unfortunately, the reduced benefits provided to the retired workers by these individual contracts became too burdensome for the surviving Company. The surviving Company was totally dependent on the energy market. With the decline in oil prices, the fabrication business, which was primarily pipeline manufacturing and construction of offshore oil and gas platforms and top sides has nearly disappeared. Presently the oil and gas pipeline facility is not operating. However, the Company is in the process of constructing top sides for Chevron Company.

The other major remaining business was the coal business. That business has also suffered severely due to the decline in energy prices.

On January 7, 1987, new management was installed at Kaiser Steel Corporation after a lengthy proxy battle. The proxy battle was initiated due to the failure of Kaiser Steel Corporation to make dividend payments to preferred shareholders.

It was apparent to new management that a Chapter 11 reorganization was needed immediately in order to have any chance to save the Company and its remaining businesses. In fact, there was no money available during the first week to meet the payroll for the following week. It was only because a customer prepaid an account (at a substantial discount) that the Company was able to meet its first payroll after January 7, 1987.

On January 25, 1987, the Board of Directors of the Company made a difficult decision that it could no longer fund the retiree's medical and health benefits. Those benefits had been costing the Company approximately $1,700,000 per month for active and retired workers and coal miners. At the time that decision was made and continuing until the present time, Kaiser Steel simply does not have adequate funds to satisfy that type of obligation. In fact, the Company has reduced its operations significantly in an attempt to minimize all costs, including payroll. Thus, Kaiser Steel is in the position that even if ordered to pay its retiree's benefits, it would be unable to comply because it has insufficient funds to satisfy its pre-petition obligations.

Approximately two weeks after the failure to fund the insurance benefits for the retired workers pursuant to the individual contracts that Kaiser had with its retired employees, Kaiser Steel filed for relief under Chapter 11. Two days later, on February 13, 1987, Kaiser Coal Corporation, a wholly owned subsidiary of Kaiser Steel Corporation also filed for protection under Chapter 11.

Kaiser Steel Corporation presently has approximately 350 employees. None of the present employees are represented by the United Steel Workers Association. There are approximately 600 employees working for Kaiser Coal Corporation in the operation of the coal mines in Raton, New Mexico and Sunnyside, Utah. Of that number, approximately 500 are represented by the United Mine Workers of America.

The present employees of Kaiser Steel Corporation and Kaiser Coal Corporation have been afforded reduced medical and disability coverages.

The Company is attempting to reorganize at the present time, in part, by generating cash by selling its coal properties. Unless and until that sale is completed, Kaiser Steel Corporation is unable to fund health benefit programs for its retiree workers at any level. The Company feels strongly that only if it has the opportunity to successfully reorganize will the retirees have any opportunity to realize substantial and continuing benefits.

One of the Company's main concerns at the present time is that the people you are trying to help by pending proposed legislation may in fact be deprived of an opportunity to receive benefits if the Company cannot reorganize. We do not desire that our retired employees be unwitting victims of what we would agree is well-intentioned legislation. However, we think it is important for you to recognize that the present legislation, if passed in its current form, could have the effect of forcing companies like Kaiser Steel into either an immediate liquidation or to prevent any chance of a successful reorganization plan being confirmed. However, we believe that the legislation could be modified to afford companies like Kaiser Steel the opportunity to reorganize without affecting the basic thrust of this legislation.

Senate-548, entitled the Retiree Benefit Security Act of 1987, is a direct outgrowth of the termination of retiree benefits by LTV Corporation when it filed a Chapter 11 petition in 1986. LTV Corp. unilaterally terminated retirement benefits affecting its employees in numerous states. Congress passed emergency stop gap legislation which forced LTV to reinstate retiree benefits and prevented other debtor-businesses from unilaterally terminating benefits until May 15, 1987. The stop gap measure is a part of the Combined Omnibus Budget Reconciliation Act of 1986. The provision was enacted without substantial congressional hearings, with virtually little publicity and with apparently little consideration given to the affect of that legislation on bankruptcy laws and the prospects for reorganization of Chapter 11 debtors. There is virtually no legislative history for this proposal.

The proposed Retiree Benefit Security Act of 1987 is intended to provide a permanent solution to the LTV Corporation problem. Supporters of the proposed legislation urge that the Bankruptcy Amendments and Federal Judgeships Act of 1984, particularly new 11 U.S.C. §1113, was intended to protect not only active workers but also retirees, and that the proposed legislation merely clarifies the scope of this coverage. Kaiser Steel believes that the proposed law amends and expands Sections 1113, 1122 and 1129, and adds a new Section 1114. It prohibits termination or modification of benefits until good faith negotiations between debtors and its unions have been conducted. If negotiations are fruitless, a hearing and court determination is required before any changes to benefits can be implemented. S.548 requires that the Bankruptcy Court must determine after a hearing that termination or reduction of benefits is necessary to permit reorganization; that all creditors, the debtor and all affected parties are treated fairly and equitably and that the balance of the equities clearly favor the entry of an order authorizing the trustee to modify the retiree benefits to the level sought by the Debtor in Possession. The proposed law also provides that retiree claims must be classified seperately from other claims and provides protection and a voice on the confirmation of the plan for retiree claimants under Section 1129.

The above noted provisions impact seriously upon Kaiser Steel's present efforts to effect a reorganization under Chapter 11 of the Bankruptcy Code.

The legislation of October 30, 1986, Public Law 99-591, may or may not apply to Kaiser Steel's relations with its retirees. However, Kaiser Steel is in serious negotiations with its retirees to try to reach an accommodation with them regarding their retiree benefits. The plain and simple matter of fact is that if Kaiser Steel would be ordered to pay all of the pre-petition retiree benefit claims that may be asserted there would be no chance whatsoever of Kaiser Steel reorganizing as a successful company. On the other hand, Kaiser Steel does have substantial assets which, if liquidated properly and in an orderly manner, would generate funds to keep the steel and coal operations going and to provide a fund of money which could be used to service the retiree claims.

We at Kaiser Steel are sensitive to the limitations of retiree's rights of an insolvent company. It is a serious problem which the Congress should rightly address. Proposals to assure adequate funding, or even to provide governmental funding are worthy of consideration. Perhaps tax incentives for pre-funding retiree death, disability and health benefits may be the answer or part of the answer. But that is not the issue for Kaiser Steel -- such proposals come too late unless Kaiser Steel does effectuate a reorganization which can provide for the needs of its retired workers.

We do not believe that the corporate reorganization provisions of Chapter 11 of the Bankruptcy Code is the place where social policy of protecting retirees should be implemented. The consequences of the proposed legislation may, in fact, discourage attempted reorganizations. The creation of new priorities may threaten secured lenders, raise the costs and decrease the availability of necessary funds to operate -- all factors that must be prejudged before a reorganization is undertaken. The addition of a large class to cost of administration priority status will severely limit the ability of Kaiser Steel to reorganize. Priority expenses must be paid in full at the time of confirmation which, in Kaiser's case, would cause a severe drain on funds available for the attempted reorganization.

Kaiser Steel must deal with its various classes of creditors. The rights of the companies secured creditors would not be impacted by S.548. The creditors affected by S.548 would be the unsecured creditors, including the current employees of the Company and those retirees whom Congress would now give a priority for their retiree benefits. We are concerned about the prospect for reorganization under the proposed legislation, a prospect which is also a concern of our current employees. The best chance the retirees of Kaiser Steel have is a successful reorganization which will provide for payment of benefits over a period of time. An order for Kaiser Steel to pay pre-petition retiree benefits as an administrative expense is an insurmountable problem to reorganization. Tragically such a requirement would lead inevitably to a liquidation under Chapter 7 if all the other unsecured creditors must defer their claims to the claims of pre-petition retireees. It is most likely, that such creditors would join with the secured claims to convert the case to a liquidation, in which case, everyone loses except possibly the secured creditors.

The present management of Kaiser recognizes that the claims of the retirees are legitimate claims. A problem, however, is that if they are given a preferred priority status over all other unsecured creditors requiring them to be paid in full, the administration of this case would be futile and there would be no reason for the reorganization efforts to go forward. Kaiser Steel simply cannot pay the benefits as mandated by the present legislation.

We suggest and urge that if the Congress intends to extend Public Law 99-591 to a date beyond May 15, 1987 or enact S.548 that it amend the provisions of that Bill to provide that the priority payment status as presently contemplated for retiree benefits be eliminated or provide that such preferential status should not commence until after the Bankruptcy Court has had an opportunity to conduct a hearing and make a determination that termination or reduction of benefits is necessary to permit reorganization.

Moreover, the requirement of maximum benefits to a separate class of retirees in a confirmed Chapter 11 plan must be eliminated as that preference at the expense of the other unsecured creditors provides a clear motivation to those other creditors and conversion of the case to Chapter 7 where this legislation does not apply. In Kaiser's case, such a conversion would only further penalize the retirees who deserve the enhanced return that a successful reorganization could provide.

Kaiser Steel Corporation and I thank you for giving us the opportunity to expre.s our views on this most serious problem which the Congress of the United States and Kaiser Steel must deal with at the same time and in the interest of the retirees.

Senator HEFLIN. Thank you, gentlemen.

Next is the National Council of Senior Citizens, Mr. William Hutton, executive director.

## STATEMENT OF WILLIAM R. HUTTON, EXECUTIVE DIRECTOR, NATIONAL COUNCIL OF SENIOR CITIZENS, ACCOMPANIED BY ENID KASSNER

Mr. HUTTON. Thank you, Mr. Chairman. I am accompanied by Ms. Enid Kassner, of our legislative department, who is particularly handling this bill.

I will, of course—my entire testimony is in, so I will just raise some highlights at this stage. I am executive director of the National Council of Senior Citizens, and I do appreciate this opportunity to speak in support of S. 548, the Retiree Benefits Security Act of 1987.

We believe this legislation would provided needed protection for retirees when a company files for bankruptcy. Last year, Congress enacted an interim measure which required employers filing for bankruptcy to continue paying such benefits until May 15. Thousands of retirees around the country are now counting the days until May 15 when, unless Congress acts, they will lose benefits which are so vital to their well-being.

Now, I know that the Senate has already passed a bill to extend this deadline. I hope that the House will rise quickly and do likewise. We have received hundreds of letters, Mr. Chairman, in the last months from retirees and their spouses whose health benefits are now in jeopardy. They are not only from Ohio and Pennsylvania, we have received letters from half the States in the Nation.

These people are asking for help and tell us that they would be devastated at the loss of medical coverage.

Just in the last 2 or 3 weeks, there are 100 letters in here that just arrived all on this subject and the people are very nervous out there. They——

Senator **Heflin**. Well, we have got volumes.

Mr. **Hutton**. I bet you have. Many of them even tell us that they learned about the cancellation of their medical benefits in the newspapers long before the companies ever wrote to them about it.

It is a simple fact that older persons require considerably more medical care than do the young, and while nearly all persons 65 and older receive Medicare, their out-of-pocket costs for health care are nevertheless three times the average amount spent by other Americans and constitute 15 percent of their income.

The promise of employer-provided health insurance in retirement can help alleviate the financial and emotional burden which is faced by older people. Private insurance for older persons is often unavailable at any price and, when available, tends to be prohibitively expensive. Retirees are fundamentally different from other creditors in the bankruptcy process. They cannot postpone receipt of medical attention if they are ill, and they usually do not have their own resources with which to replace lost benefits, and they have little leverage to assert their needs with the company for they are no longer providing a needed service for that company.

There is one group of retirees for whom the disruption of bankruptcy has been particularly devastating, those who retired early. As the LTV Corp. and its many subsidiaries began to face economic distress, large numbers of older workers were asked to retire early to make way for younger workers and "for the good of the company." Others were forced into early retirement due to plant closings. These persons, often in their late fifties or early sixties, were promised pension supplements to help them until age 62 when they could apply for social security. They were also promised health and life insurance.

For this group of people, who were made a whole smash of promises and that was all, health benefits are an absolute necessity. Medicare eligibility does not begin until the age of 65. These early retirees are having a hard time finding new jobs as employment opportunities are scarce for older workers, especially in economically depressed areas. Some have found jobs at the minimum wage, but such jobs generally offer no employee benefits.

Over and over, the retirees affected have expressed dismay that the company is "hiding in bankruptcy" while their lives have been thrown into turmoil. They do not want welfare. They only want the benefits they were promised.

NCSC supports S. 548 for the following reasons:

First, the bill clarifies that retiree benefits must receive the same protection as other collectively bargained agreements. This action would prevent the unilateral termination of retiree benefits by a company when filing for bankruptcy.

Second, S. 548 would protect against any unilateral termination or modification of retiree benefits regardless of whether or not they were collectively bargained. This measure would help protect the benefits of nonunion as well as union retirees.

Third, the court could only order a modification of retiree benefits after finding such action necessary to permit the company's reorganization and, then, such modification would have to be fair and equitable to all parties.

NCSC has long called for the establishment of a universal, comprehensive, national health plan for all Americans, Mr. Chairman, and in the long run, we continue to believe that a national program will be the best means of protecting all our citizens. But for the immediate future, we urge the members of this subcommittee to protect the benefits of retirees by approving S. 548.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Hutton follows:]

# Statement

# of

William R. Hutton
Executive Director
National Council of Senior Citizens

Good morning Chairman Heflin and Members of the Subcommittee. I am William R. Hutton, Executive Director of the National Council of Senior Citizens. I appreciate this opportunity to speak in support of S. 548, the Retiree Benefits Security Act of 1987. We believe this legislation will provide needed protection for retirees when a company files for bankruptcy.

The issue at stake here is one of fundamental decency and addresses the need for corporations to responsibly honor commitments made to their employees. I know the members of the Subcommittee are all aware that this issue first received broad public attention when the LTV Corporation filed for bankruptcy and declared its intention to terminate retiree health and life insurance benefits.

Last year, Congress enacted an interim measure which required employers filing for bankruptcy to continue paying such benefits until May 15, 1987. Thousands of retirees around the country are now counting the days until May 15, aware that, unless Congress acts, they will lose benefits which are vital to their well-being.

Although the LTV situation has been the most visible case, the problem is not confined to those retirees. NCSC has received hundreds of letters from retirees and their spouses whose health benefits are now in jeopardy. They are not only from Ohio and Pennsylvania; we have received letters from half the states in the nation. These people are asking for help and tell us they will be devastated by the loss of medical coverage.

It is a simple fact that older persons require considerably more medical care than do the young. While nearly all persons 65 and older receive Medicare, their out-of-pocket costs for health care are, nevertheless, three times the average amount spent by other Americans and constitute 15 percent of their income.

The promise of employer-provided health insurance in retirement can help alleviate the financial and emotional burden faced by older persons. Private insurance for older persons is often unavailable at any price and, when available, tends to be prohibitively expensive.

Retirees are fundamentally different from other creditors in the bankruptcy process. They cannot postpone receipt of medical attention if they are ill. They usually do not have their own resources with which to replace lost benefits. And, they have little leverage to assert their needs with the company, for they are no longer providing a needed service.

Rather, they have already completed their obligations by having contributed years of labor to the company. Many retirees now feel that the companies for which they devoted years of their lives are ready to cast them aside.

There is one group of retirees for whom the disruption of bankruptcy has been particularly devastating--those who retired early. As the LTV Corporation and its many subsidiaries began to face economic distress, large numbers of older workers were asked to retire early to make way for younger workers and "for the good of the company." Others were forced into early retirement due to plant closings. These persons, often in their late 50s or early 60s, were promised pension supplements to help them until age 62, when they could apply for Social Security. They were also promised health and life insurance. For this group of people, health benefits are an absolute necessity, since Medicare eligibility does not begin until the age of 65.

As important as health benefits are as a supplement to Medicare, they are essential for older persons with no other coverage. Some of our members have told us that it will cost them $2,000 a year to obtain health insurance--an amount they cannot afford, especially now that their pensions have been drastically reduced.

These early retirees are having a hard time finding new jobs, as employment opportunities are scarce for older workers--especially in economically depressed areas. Some have found jobs at the minimum wage, but such jobs generally offer no employee benefits.

Over and over, the retirees affected have expressed dismay that the company is "hiding in bankruptcy," while their lives have been thrown into turmoil. They do not want welfare; they only want the benefits they were promised.

NCSC supports S. 548 for the following reasons:

First, the bill clarifies that retiree benefits must receive the same protection as other collectively bargained agreements. This action would prevent the unilateral termination of retiree benefits by a company when filing for bankruptcy. An employer would have to first bargain with the union before seeking court action to reject a collectively bargained agreement. Several companies have claimed that current law required them to terminate such benefits upon declaring bankruptcy, which indicates that this clarification is necessary.

Second, S. 548 would add a new Section 1114 to the Bankruptcy Code which would protect against any unilateral termination or modification of retiree benefits regardless of whether or not they were collectively bargained. This measure would help protect the benefits of non-union as well as union retirees.

Third, the court could only order a modification of retiree benefits after finding such action necessary to permit the company's reorganization and, then, such modification would have to be fair and equitable to all parties.

Finally, retirees would constitute a separate class for voting purposes. This would give the claims of retirees extra weight in the settlement process. As such, the reasonable claims of retirees could prevent the approval of an unfair settlement.

NCSC believes S. 548 takes an important first step in protecting retirees, but other actions are also needed. Any early retirees who lose promised health benefits should, at least, be provided with Medicaid coverage until they are old enough for Medicare.

Furthermore, NCSC has long called for the establishment of a universal, comprehensive, national health plan for all Americans. In the long run, we continue to believe that a national health program is the best means of protecting all our citizens from the anxiety and financial burden of a medical emergency.

But for the immediate future, we urge the members of this Subcommittee to act before the May 15 deadline to protect the benefits of retirees by approving S. 548.

Senator HEFLIN. You suggested that Congress pass legislation to provide Medicaid coverage to early retirees who have lost promised health benefits until they are eligible to receive Medicare. Do you have any statistics on what percentage of the retirees would fall in this category?

Ms. KASSNER. I believe there is something in the area of 20,000 retirees who are affected.

Senator HEFLIN. What percentage is that? Is that 10, 15, 20, 30, 40, or what? Do you have any ballpark percentage figure?

Mr. HUTTON. Well, LTV is about 82,000, and 20,000 affected would be approximately 25 percent.

Senator HEFLIN. Do you have any projections on how much a program such as this might cost?

Ms. KASSNER. We do not have an estimate at this time.

Senator HEFLIN. Senator Metzenbaum?

Senator METZENBAUM. I have no questions.

Senator HEFLIN. Thank you.

Senator METZENBAUM. It is good to see you again.

Mr. HUTTON. Thank you, Senator.

Senator HEFLIN. We call our next witness, Mr. Hubert H. Humphrey III, attorney general of the State of Minnesota.

Mr. Humphrey, we are delighted to see you here and we look forward to hearing your testimony.

## STATEMENT OF HUBERT H. HUMPHREY III, ATTORNEY GENERAL, STATE OF MINNESOTA

Mr. HUMPHREY. Thank you, Mr. Chairman, and I want to thank you and the members of the committee and your staff for the courtesy of arranging the time so that I can get here on time from Minnesota. I appreciate——

Senator METZENBAUM. I am going to walk out on your testimony only because I must be on time to a 12 o'clock luncheon; it is no personal offense. I looked forward to hearing from you.

Mr. HUMPHREY. Absolutely not, Senator. I appreciate the opportunity to be here and I want to let you know that I am very strongly in support of this legislation. I think it will help very much the particular situation or at least not allow similar circumstances now happening in Minnesota to happen elsewhere, and I want to inform the committee about that.

Mr. Chairman and Senator, I do have formal comment. I will try and not go directly through those comments, but I do want to highlight just a few if I possibly could. I know that we are short on time and so I will try and keep my comments to a minimum.

I want to thank you, Mr. Chairman and members of the subcommittee, for the opportunity to share with you my views of support for S. 548, the Retiree Benefits Security Act of 1987.

In Minnesota, as in many other States, chapter 11 debtors have used the Bankruptcy Code to suddenly terminate medical and disability benefits for retirees. These retirees need and deserve protection and the assistance of Congress and therefore I urge that you take swift action for passage of this legislation.

As members of the subcommittee know, I am sure, this bill is in part a legislative response to the LTV situation, that is, LTV's decision last year to stop paying all nonpension retirement benefits to its 78,000 retirees.

Now, happily, Mr. Chairman, in that circumstance, of course, the steelworkers strike in East Chicago convinced LTV to restore those benefits for 6 months and later Congress did take action, passing legislation requiring the continuation of the retiree benefits until May 15, 1987. So for at least the moment the individuals are receiving benefits they were promised and on which they depend.

I wish I could report to you that the circumstances in Minnesota were the same. In Minnesota's Iron Range, however, the picture has been much more bleak. Three weeks after LTV filed for chapter 11 protection, Reserve Mining Co. also went bankrupt, leaving thousands of retirees without benefits. LTV is a partner in that bankruptcy.

Neither the LTV Steelworkers agreement nor the LTV bill enacted last fall have done anything for this group of retirees and for many of them the situation is now getting very desperate.

Mr. Chairman, since last August I have had the opportunity to hear from families with tens of thousands of dollars in unpaid medical bills and no way to make even a dent in these obligations. I have traveled to northeastern Minnesota and been there a number of times to observe mining towns of Silver Bay and Babbitt, and I have seen the fear and the frustration in the faces of people who have given their entire working lives to the company and have relied on the company's promises and now they do not know where to turn. They are in a desperate situation and, in fact, the plant gates are being picketed and we are getting into a much more intense situation.

Now, despite the real human hardship right now in Minnesota's Iron Range, this is hardly a single State or even a region's particular problem. As the Senate Special Committee on Aging reported last August, employer-sponsored retiree health benefits represent the only health care coverage for many millions of individuals.

I will not go through, Mr. Chairman, the detail on that report, but I think it relates very directly to this kind of situation and something that I hope the committee will take into account.

There is a situation in which these individuals are highly dependent and this bill, S. 548, does a great deal to address that imbalance of power. Instead of penalizing or even requiring the abrupt termination of all benefits at the moment a chapter 11 petition is filed, section 114(d) of this bill, of course, provides that the debtor in possession or a trustee in a chapter 11 case cannot modify any retiree benefits except through agreement with the retirees' representative or court order. I think that is quite appropriate, Mr. Chairman.

Under the bill, the bankruptcy court can permit modifications only if it can find that the proposed modifications are necessary to permit the reorganization of the debtor and assure that all creditors and debtors and all of the affected parties are treated fairly and equitably. That is basically the same standard as the procedure for modifying collective bargaining agreements under section 1113, and it represents, really, Mr. Chairman, a fair balance between the goals of ERISA and the Bankruptcy Code.

I understand that there are, of course, a number of employer groups and bankruptcy attorneys that oppose this bill on the grounds that it will make successful reorganization impossible, and I think you just heard from several of those. They claim that this proposal, by elevating retiree claims above other claims, introduces an element of rigidity into the bankruptcy process that will frustrate its purpose of allowing the companies a fresh start.

Well, I think there are at least two responses, Mr. Chairman, to that kind of complaint. First of all, the bill itself provides a number of safety valves for those situations where maintaining retiree benefits will truly cripple the reorganization effort. I will not go through those specific items, but they are outlined very directly in the bill, providing for an opportunity when there are those circumstances where the court would agree that reorganization could not take place without a court order which would reduce those benefits. So there are those circumstances where there can be a showing upon hearing that reorganization cannot go forward if the full benefits are paid.

Retirees also play a very active role in this and they understand that it is in their best interest, it is in the mutual interest not only of the company to survive but certainly the retirees to survive, and so retirees understand that their best protection against loss of benefits is an employer continuing to operate a profitable business and they can certainly be expected to make reasonable efforts to reach their compromises. And I have seen that very directly, the efforts of the retirees of Reserve Mining working as hard as they possibly can, both with the organized steelworkers as well as in their own organizations, to try and come to grips with some form of agreement, and they understand that the interests of the company surviving is in their very best interests.

Second, Mr. Chairman, it is simply not true, as some employers and bankruptcy attorneys seem to assume, that all creditors are or should be equally situated. Banks usually do not care if they are paid now, rather than a year from now, so long as they recover the entire value of their money. Now, retirees, on the other hand, do not have that luxury of time. They are relatively powerless to protect themselves, they are not in a position to wait, they need the benefits now, and if they must take a reduction to permit the company to survive, they need bargaining leverage to avoid being lumped together with the general unsecured creditors, and if all else fails they need time to find alternative coverage.

Mr. Chairman, time is of the essence for retirees. They are up against the wall, they have a priority need for the health care benefits immediately. That is the dire circumstances that retirees find themselves in.

I believe that S. 548 gives them a better opportunity, gives them the leverage that they need to become an active participant in seeing that the reorganization takes place. It allows them to survive the process of reorganization. Creditors may have some difficulty, but they are going to survive. They are not in retirement. They are in trouble, but they are not in retirement. The retirees are in retirement and every single day of their lives is very valuable and the costs are immense, health and emotional and otherwise.

Mr. Chairman, I hope that you can take direct action on this piece of legislation.

Thank you very much.

[Submissions of Mr. Humphrey follow:]

# STATEMENT OF HUBERT H. HUMPHREY, III MINNESOTA ATTORNEY GENERAL, IN SUPPORT OF S.548, THE RETIREE BENEFITS SECURITY ACT OF 1987

April 24, 1987

Thank you, Chairman Heflin, Senator Metzenbaum, and members of the Subcommittee on Courts and Administrative Practice, for the opportunity to submit a statement in support of S.548, the Retiree Benefits Security Act of 1987. In Minnesota, as in many other states, chapter 11 debtors have used the bankruptcy code to suddenly terminate medical and disability benefits for retirees. These people need and deserve the protection and assistance of Congress, and therefore, I urge swift passage of this legislation.

As the members of this subcommittee know, this bill is, in part, a legislative response to LTV's decision last year to stop paying all non-pension retirement benefits to its 73,000 retirees. Happily, the Steelworkers strike in East Chicago convinced LTV to restore those benefits for six months, and later, Congress passed legislation requiring the continuation of retiree benefits until May 15, 1987. For the moment, at least, those individuals are receiving the benefits they were promised and or which they depend.

In Minnesota's Iron Range, however, the picture has been much more bleak. Three weeks after LTV filed for chapter 11 protection, Reserve Mining Company also went bankrupt, leaving thousands of retirees without medical benefits. Neither the LTV/Steelworkers agreement nor the "LTV bill" enacted last fall have done a thing for this group of retirees and, for many of them, the situation is now getting desperate.

Since last August, I have heard from families with tens of thousands of dollars in unpaid medical bills and no way to make even a dent in their obligations. I have traveled a number of times to the Reserve Mining towns of Silver Bay and Babbitt, and

I have seen the fear and the frustration in the faces of people who have given their entire working lives to the company, have relied on the company's promises, and now don't know where to turn.

Despite the real human hardship right now on Minnesota's Iron Range, this is hardly a regional problem. As the Senate Special Committee on Aging reported last August, employer-sponsored retiree health benefits represent the only health care coverage for three million retirees under 65 and are a critical supplement to Medicare for more than twice that number over 65. Continued health coverage for retirees is promised to 84 percent of employees of large firms and nearly half of those working for firms with 100 - 250 employees. Those individuals understandably rely on their employer's promises of lifetime benefits, and they rarely, if ever, maintain any individual coverage to cover the possible termination of their employer-paid benefits.

Once these people actually reach retirement age, it is usually too late to get adequate individual policies. To pay the premiums for an individual policy, couples age 62-64 would have to spend an average of 56 percent of their social security benefits if that were their only source of income. Those with pensions would still have to pay 35 percent of their retirement income in health insurance premiums. Of course, that only counts those retirees that can get insurance at all. Many have medical conditions at the time of retirement that render them altogether uninsurable.

Despite the utterly dependent situation of these people, the law has done little to protect them. Only recently have the federal courts begun to use their power to fashion federal common law under the Employee Retirement Income Security Act (ERISA) to enforce the terms of retiree health benefit packages. In the bankruptcy context, the protections for retirees are even more limited. Even if they can establish an enforceable obligation to pay benefits on the part of their employer, they face the argument that retiree benefits are pre-petition obligations that cannot be paid by a debtor absent assumption of a contract under section 365 of the Bankruptcy Code or some other court-approved procedure. If they can survive until the end of the reorganization process, which can, as all of you know, take years, they are, at best, entitled only to a low priority among the unsecured creditors. Those with unpaid medical expenses totalling more than $2,000 simply join the pool of general unsecured creditors to allege and face a substantial risk of collecting nothing.

This bill does a great deal to address this imbalance of power. Instead of penalizing (or even requiring) the abrupt termination of all benefits at the moment the chapter 11 petition is filed, section 1114(d) provides that a debtor in possession or a trustee in a chapter 11 case cannot modify any retiree benefits except through agreement with the retirees' representative or by court order. The bankruptcy court can permit modification only if it can find that the proposed modifications are "necessary to permit the reorganization of the debtor and assure that all creditors, the debtor, and all of the affected parties are treated fairly and equitably; and the balance of equities clearly favors the entry of an order authorizing" the changes. That is basically the same standard as the procedure for modifying collective bargaining agreements under section 1113, and it represents a fair balance between the goals of ERISA and the bankruptcy code.

I understand that a number of employer groups and bankruptcy attorneys oppose this bill on the grounds that it will make successful reorganizations impossible. They claim that this proposal, by elevating retiree claims above other claims, introduces an element of rigidity into the bankruptcy process that will frustrate its purpose of allowing companies a "fresh start." There are, I think, at least two responses to that argument.

First of all, the bill itself provides a number of safety valves for those situations where maintaining retiree benefits will truly cripple the reorganization effort. Section 1114(g) permits a debtor to obtain a court order implementing interim changes in retiree benefits "if essential to the continuation of the debtor's business or in order to avoid irreparable damage to the estate." Section 1114(e) and (f) permit the court to order more permanent modifications if "necessary to permit the reorganization of the debtor" and, of course, retirees may well agree to changes if they know that the company will not otherwise survive. Retirees understand that their best protection against loss of benefits is an employer continuing to operate a profitable business, and they can be expected to make reasonable efforts to reach fair compromises.

Second, it simply is not true, as some employers and bankruptcy attorneys seem to assume, that all creditors are or should be equally situated. Banks usually do not care if they are paid now rather than a year from now, so long as they recover the time value of their money. Retirees, on the other hand, do not have that luxury. They are relatively powerless to protect themselves, and they are not in a position to wait. They need the benefits now, and, if they must take a reduction to permit the company to survive, they need bargaining leverage to avoid being lumped together with the general unsecured creditors and, if all else fails, they need time to find alternative coverage.

Too often, as the Senate Special Committee on Aging concluded, retirees suddenly find the promise of health benefits for life is a promise a company can break "with the click of a lock on the factory gate or the bang of a door on the bankruptcy court." The Retiree Benefit Protection Act of 1987 is a good first step toward solving this problem, and I urge its speedy enactment.

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HUBERT H. HUMPHREY, III
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May 11, 1987

The Honorable Howell Heflin
United States Senate
Washington, D.C. 20510

Re: S.548 -- Retiree Benefit Security Act

Dear Senator Heflin:

Thank you and the members of the Senate Subcommittee on Courts and Administrative Practice for permitting me to testify on behalf of the Retiree Benefits Security Act. I hope the subcommittee takes speedy action to move this bill forward.

On May 8, I received your letter asking whether the State of Minnesota has taken any actions to alleviate the pain and suffering the retirees from Reserve Mining Company are facing. We have been trying a number of different approaches.

1. Emergency relief program: Almost immediately after the Reserve bankruptcy filing last August, we worked with the Steelworkers union to negotiate a $500,000 catastrophic insurance package with Armco Steel, one of Reserve's partners. That helped for awhile, but those funds were quickly exhausted.

2. Organization: We sponsored the formation of hourly and salaried retiree associations and helped these groups to secure counsel to represent them in the bankruptcy proceedings. Since we would have difficulty establishing standing in the bankruptcy court to represent retirees and would have problems avoiding conflicts of interest down the road, we could not represent the retirees directly. Nevertheless, to ensure that the retirees would be able to negotiate effectively, we helped them form their own organizations.

3. Negotiation: The Steelworkers negotiated an agreement with the Reserve trustee that would allocate a portion of asset and inventory sale proceeds to a medical insurance trust fund. Unfortunately, as the bankruptcy code now permits, the secured creditors objected and insisted that all sale proceeds be directed to Reserve's bondholders. To try to meet that

objection, we intervened in the negotiations to try to provide adequate protection to the secured creditors in the form of foregone setoff claims so that the Steelworkers agreement could be approved. To date, the secured creditors have been adamant, but we remain optimistic that an arrangement can be worked out. The priority that secured creditors have over retiree claims under the present bankruptcy code has proven to be a formidable obstacle.

4. Legal assistance: From the beginning, we have pledged to assist the union or the retiree associations in pressing any claims they might have under Section 1113 of the bankruptcy code or under ERISA. Working with Congressman Oberstar's office, we helped to draft the "LTV legislation" mandating the continuation of retiree benefits until May 15 (now September 15 under the new amendment). To the extent our state laws give us the authority, we have tried to halt abusive practices by the retirees' creditors and we have encouraged clinics and hospitals to give these people more breathing space.

The one thing we have not done is provide direct state subsidies to the retirees. First of all, that would require state legislation, an unlikely prospect given the hundreds of thousands of other Minnesotans who do not have health insurance. Moreover, since the State cannot create a new claim after the bankruptcy filing, such a subsidy might well let the steel companies off the hook. The obligation to pay retiree benefits is theirs, and the Retiree Benefits Security Act is needed to make them live up to their bargain.

If you need additional information, please let me know.

Best regards,

Hubert H. Humphrey III

HUBERT H. HUMPHREY, III
Attorney General

HHH/mm
cc: David Starr

Senator HEFLIN. Thank you, Mr. Humphrey. We appreciate your testimony, your understanding of a very complex phase of law. We are always delighted to see people who deal with State matters that have some understanding of the complexity of Federal matters as they come before us.

You mentioned in some broad sense the reorganization that is available for companies who get into financial distress. We have many steel companies, many companies here today that are in financial distress as a result of ill-conceived policy, and as a result of foreign subsidies dumping, as we call it, in States where the foreign countries are making the steel companies sell at below the cost of production in this country. There are a lot of problems of this kind.

But the bankruptcy court does allow for a period to reorganize the company, to give them some breathing time and certain tools of reorganization. But it strikes me that retirees who have reached a certain age have little ability to reorganize on a comparative basis. Would you speak to the reorganizational ability of a retiree as compared to a business?

Mr. HUMPHREY. Well, Mr. Chairman, again I have to first of all respond to your question with the emotion that I see in the eyes of people that I have visited with. They are desperate. In their own efforts of reorganizing, they make very, very strong efforts to try and find private coverage. They make very strong efforts to come to their legislatures, State legislatures to try and find some assistance if that is possible. They try and work out with their neighbors and their friends and the other members of their families, but they are always in a very desperate situation in these kinds of circumstances, and I do have to refer back to the report of the Senate Special Committee on Aging, because I really think that sets out the kind of numbers that show the dependency of these individuals.

If you note, for instance, that employer-sponsored retiree health benefits represent the only health care coverage for 3 million retirees before age 65 and are a critical supplement to Medicare for more than twice that number after 65. This is really their nest egg. This is the thing they are depending on. They have their home and then they hopefully have their benefits. I can tell you, in the Reserve situation their home is not worth anything. That is the only company in town basically. Everything else lives off of Reserve Mining up there, and when you try and sell—if you want to get yourself a nice beautiful retirement home on Lake Superior, I can tell you, there are plenty of them that are available in the town along the lakeshore there.

The other part of it is that when you cut out the health care benefits, you have really taken whatever basis for reorganizing their own lives away from them. This is something that they have attempted to rely on. In fact, many of the people at Reserve, Mr. Chairman, were led to retire early specifically and given additional benefits so that their company could hopefully stay out of this sort of circumstance. They were given not only promises, they had regular retirement, they were lured and told that if they will retire so that the company can take on younger employees, so it can pay less, then it will be in a better shape, and so now once again a double whammy, they get beat up.

And I would just daresay, Mr. Chairman, that the details could easily be looked at with the numbers of individuals that have been significantly impacted in this situation.

Senator HEFLIN. Thank you, Mr. Humphrey. We appreciate your testimony as well as the testimony of all of our witnesses today.

I would like to announce that the record will be held open until the close of business on May 1 for those who wish to submit a written statement.

There may be additional questions that will be asked of the witnesses in writing and, if so, we would appreciate a prompt response to those questions.

So with this, we will now conclude the hearing. Thank you very much.

[Whereupon, at 12:08 p.m., the subcommittee adjourned.]

# APPENDIX

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## ADDITIONAL STATEMENTS

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American Council of Life Insurance

May 27, 1987

Senator Howell Heflin
Subcommittee on Courts and
  Administrative Practice
U.S. Senate
223 Senate Hart Office Building
Washington, D.C.  20510

Dear Senator Heflin:

I am Chairman of the Subcommittee on Federal Bankruptcy Legislation of the American Council of Life Insurance. After submission of the Council's statement of May 14, 1987 on S. 548, we have been meeting with Subcommittee staff on the proposed revision and now have some additional comments to make. We appreciate the courtesies that have been extended to us by the Committee and staff, and this opportunity to further clarify our position. We are enclosing a second redraft of our statement correcting several typographical errors and making the following two substantive changes:

1. S. 548 Should Deal Only With Retiree Benefits as Defined in Proposed Section 1114(a).

   It was our understanding that the parenthetical clause in the original Section 2(a) of S. 548 was intended to apply to retiree benefits as defined in Section 1114(a). We now understand that the parenthetical clause in Section 2(a) is intended by the draftsmen to go beyond the Section 1114(a) definition to include pension benefits. Since pension benefits are covered by ERISA, we are opposed to expanding S. 548 to cover such benefits, and suggest deletion of Section 2(a) of S. 548. In the alternative, the clause might be modified to conform it to the Section 1114(a) definition.

2. Council Position Should Not be Interpreted to Support Creating Claims Where There Is No Obligation to Provide Benefits.

In the Council's statement of May 14, 1987, we failed to delete a reference to a provision on Page 7 (no longer contained in our proposed bill) which would have limited claims of employees under non-collectively bargained plans to the cost of Medicare coverage, where the agreement to provide benefits was not covered by a contract directly between the employee and the company. This provision had been deleted, *inter alia*, because it placed non-union employees at a disadvantage. Since the reference on Page 7 creates an ambiguity in the absence of the now deleted statutory language, we would like to emphasize that the Council did not, in its original suggestion, nor does it now, support the granting of a claim where there is no contractual obligation to provide benefits.

Thank you very much for your kind consideration. If we can be of any further assistance, please do not hesitate to call on us.

Sincerely,

R. M. Zinman

Robert M. Zinman tlw

cc: Ms. Karen Kremer, Chief Counsel

RMZ/tlw

# STATEMENT OF THE
# AMERICAN COUNCIL OF LIFE INSURANCE
for the
SENATE JUDICIARY SUBCOMMITTEE
on
COURTS AND ADMINISTRATIVE PRACTICE
on
S. 548
THE RETIREE BENEFITS SECURITY ACT

May 26, 1987 REVISED STATEMENT

seek to expedite the successful reorganization of the firm

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The American Council of Life Insurance (Council) is a trade association with a membership of 629 life insurance companies. In the aggregate, these companies account for approximately 95 percent of the life insurance in force in the United States and hold 96 percent of the assets of insured pension plans.

Policy positions of the Council are set by the Board of Directors with the assistance of over 62 committees and subcommittees, each with responsibility in a specific subject area. Membership in the Council's committees totals more than 500 company officers and other executives -- experts in their fields -- who represent a cross-section of the business. The Council appreciates this opportunity to submit comments concerning S. 548, the Retiree Benefits Security Act of 1987.

## COUNCIL IN UNIQUE POSITION TO EXAMINE LEGISLATION

As major group benefit underwriters of retiree benefit plans and as major creditors of firms with retiree benefit plans, the Council believes that it is uniquely qualified to examine this legislation in a calm and dispassionate manner. The Council is aware that while our members stand to benefit from this legislation to the extent that it enables corporations to keep in force retiree life and health insurance underwritten by our members, our members stand in the position of unsecured creditors, whose interests would be adversely affected by the bill.

The Council recognizes that millions of retired Americans count upon the life, health, and disability insurance provided to them by their former employers. For those under 65, it may be their primary source for health insurance. For those over 65, it supplements a medicare health plan. Clearly, this insurance represents an important and necessary element of

5/26/87

their retirement. However, for some, their retirement plans are threatened by the prospect that the former employer may find it necessary to terminate these benefits while it seeks financial protection from creditors through bankruptcy. When this occurs, questions arise over the obligation of the former employer to continue these benefits. Any solution to this problem must take into account the needs of the retirees as well as the legitimate claims of creditors of the debtor.

## SUMMARY OF COUNCIL POSITION

### 1. S. 548 Should Not Be Enacted In Its Present Form.

The Council recognizes the very real concern for the plight of retired workers of companies in bankruptcy proceedings that motivates S. 548 and the need for prompt action to resolve this crisis. Nevertheless, reluctantly, we must express our opposition to the enactment of S. 548 in its present form because of the impact it will have on creditors, existing employees, the retirees themselves, as well as the efficient administration of the bankruptcy machinery of the Nation.

### 2. The Council Opposes Further Continuation Legislation after September 15, 1987.

In response to some very large bankruptcy reorganization applications, Congress has required firms to continue retiree benefits through May 15, 1987 and, assuming Presidential approval of S. 903, through September 15, 1987. The Council recognizes the need to deal with the problem on an interim basis. However, we view a simple mandate to continue these benefits as a not wholly satisfactory response since it fails to balance the competing interests of retirees with those of creditors, employees, and managers of the firm, all of whom seek to expedite the successful reorganization of the firm pursuant to the Bankruptcy Code. It is, therefore, imperative that a long term solution that recognizes the interests of all parties to the reorganization be adopted before September 15th.

3. The Council supports modifications of S. 548 that will Fairly Balance The Interests Of All Parties Competing For Funds In Reorganizations.

The proposed modifications provide for an automatic sixty day continuation of benefits and an opportunity for employees to purchase at group rates supplementary coverage, because of modification of benefits thereafter; provide parity for most retiree benefit claimants with other unsecured creditors; and remove the administrative expense claim for certain benefits.

4. The Council Proposes Changes To The Internal Revenue Code to Remove Disincentives to Funding of Benefits.

The proposed changes would eliminate the prohibition against using anticipated medical cost increases in determining the size of the reserve held for employees as well as the tax imposed on the employer for income received from the investment of those reserves.

## WHY THE COUNCIL DOES NOT SUPPORT S. 548 AS DRAFTED

Notwithstanding the justified concern for retired workers motivating this proposal, the Council must respectfully and regretfully disagree with the approach taken by S.548, which places the burden of paying for the retirees' life and health coverage on unsecured creditors in reorganization. The Council believes that this approach, if enacted into law, would have a severe negative impact on the ability to rehabilitate

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corporations in Chapter 11, thus resulting in loss of jobs in corporations that cannot be reorganized and tightening of credit for healthy corporations. In the end, we believe the proposal would fail to accomplish its purpose and intensify the crisis it was drafted to ameliorate.

Under S. 548, a separate class of creditors is created for retirees having claims for future health and life benefits. These retirees, would be paid in full before payments could be made to unsecured creditors under the structure of the amended Section 1129. Unsecured creditors are normally protected in a "cram down" (or court imposed plan of reorganization), only to the extent that they must be paid in full before anyone junior receives any property. Thus, the mandatory payments to the retiree class would necessarily have to be paid out of the share that would normally have gone to the unsecured creditors.

As stated by Richard Gitlin, President of the American Bankruptcy Institute, at this Subcommittee's hearing held on April 1st, the language of Section 2(e) of S.548 in this respect is ambiguous and not easily understood. However, it would seem that this Section permits the present valuing of the retiree's claims and payment in cash; the continuation of the benefits, perhaps at some reduced amount necessary to permit such continuance in the future; or a combination of the foregoing. Regardless of whether the payments are made to the retiree class or the insurance is continued, the result will be that far fewer assets will be available for distribution to unsecured creditors. Indeed, given the magnitude of unfunded life and health benefits, it may be highly unlikely that anything would be available for unsecured creditors or that the reorganized company could have economic viability.

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In addition to the foregoing, claims of retirees for health and life benefits required to be paid during the reorganization are given administrative expense treatment, which means that funds which might have been available for unsecured creditors under a plan after paying the new retiree class, now would go first to pay the retiree claims during reorganization. In fact, these claims would be paid even ahead of the claims of current workers who do not have such a priority!

The Council is concerned that this proposal, if enacted, could have severe adverse affects, including:

1. Reorganization Less Likely. S. 548 would make successful reorganization less likely, with obvious adverse impact on the national economy and on the ability of current employees to keep their jobs, or be paid their claims.

2. Unsecured Debt Wiped Out. If enacted, the proposal would wipe out vast amounts of unsecured debts. These debts represent not only investments made on behalf of pension funds, life insurance policyholders and the like, but also obligations to trade creditors and suppliers whose economic viability, including their ability to pay their employees, depends on having their claims paid; and obligations to the current employees of the debtors whose claims, already limited by Scction 502 (6) (7), may be wiped out by this legislation.

3 Less Financing for Healthy Corporations. In its present form, S. 548 would severely cripple the ability of even healthy American corporations to receive financing for development and expansion, since the liability of the corporation for these unfunded

retiree benefits and the priority created in reorganization therefor would have to be factored into the economic analysis of the corporation to determine its acceptability for financing.

4 Reduced Benefits for the Future. The proposal would force corporations to reduce or refuse to initiate or increase health and life insurance benefits to employees in order to improve their ability to obtain financing for development and expansion. (Paradoxicaly, by encouraging employers to reconsider what kind of benefits they are willing and can afford to pay to retirees, future generations of retirees may find that they may not receive the benefits in good times, that Congress has mandated be preserved for their parents in reorganization).

5 Damage Bankruptpcy Machinery. S. 548 would set the precedent of special treatment for a specific class of creditors that will lead to the destruction of the unique effectiveness of Chapter 11, which, alone in the world, permits the successful rehabilitaion, rather than the liquidation of corporations in bankruptcy.

Given the sense of justice that motivates this proposed legislation, it is extremely difficult for the Council to oppose its enactment. However, it is the Council's considered opinion the it is possible to achieve a fair solution that would afford reasonable protection to retirees without destroying the legitimate expectations of unsecured creditors and the reorganization process.

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## THE COUNCIL PROPOSAL

The Council proposal is designed to balance the interests of the various parties involved in reorganizations; to recognize the rights of retirees in Chapter 11 proceedings; to expedite the resolution of current uncertainty; and to preserve the fundamental objective of successful financial reorganization under the Bankruptcy Code.

To this end the Proposal:

1. Clarifies the obligations of retiree representatives;

2. Establishes a 60 day continuation of retiree benefits without modification from the date of the petition;

3. Provides for a further continuation of benefits throughout the reorganization process on a modified basis as directed by the bankruptcy court pursuant to standards set forth S.548 as submitted, with employees having the option to purchase supplemental coverage at group rates;

4. Eliminates the priority afforded to the retirees over unsecured creditors.

5. Eliminates the administrative expense claim for benefits required to be paid during the reorganization process, recognizing that the benefits are required to be paid by the amended proposal and will be paid to the extent the debtor has the funds to pay them.

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6. Removes existing statutory disincentives to funding retiree benefits.

The Council recognizes that the real answer to the plight of retirees is clearly a non-bankruptcy solution involving the funding of benefits during the years of employment. In this context it seems incredible that changes in the tax law in recent years have actually enacted severe disincentives to the funding of these benefits by healthy corporations.

The Council proposal removes these disincentives to funding but recognizes that funding alone is not the whole answer--certainly not for companies in current difficulties that are not in a position to fund health and life insurance benefits. The proposal provides a reasonable basis for the sharing of the reorganization risks without destroying the economic vitality of our system, while we work toward the full funding of retiree benefits.

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## NOTES TO PROPOSED REVISION

| Provisions of Bankruptcy Code Modified by S.548 | Change and Reasons Therefor |
|---|---|
| Sec. 1113(f) | Section 2.(a) of S.548 is deleted in order to remove the parenthetical clause. |
| Sec. 1113(g) | Deleted. Section 502(b)(7) is amended in Section "(e)" of proposed revision. (See changes to Section 502(b) below.) |
| Sec. 1113(i) | Changed to (h) and protection added for retired employee serving as representative. |
| Sec. 1114(c) | Protection added for retired employee serving as representative. |
| Sec. 1114(d)(1) | Mandates continuance of benefits for 60 days, before modification. |
| Sec. 1114(d)(2) | Deleted. Eliminates administrative expense treatment for benefits required to be paid during the proceeding. |
| Sec. 1114(d)(2) (New) | Added. Provides for employee purchase at group rates of supplementary benefits after modification and for payment of premiums on retained coverage. |
| Sec. 1114(f) | Deleted and combined with (e). Makes procedure standard for claimants regardless of whether collective bargaining agreement applicable. |
| Sec. 1114(g)(1) | Relettered (f)(1). Permits interim changes after 60 day post-filing period regardless of whether collective bargaining agreement is applicable. |
| Sec. 1114(i) | Deleted. Section 502(b)(7) is amended in section "(e)" of proposed revision (See change to Section 502(b) below). |
| Sec. 1122 | Places retirees in same class as other unsecured creditors. |
| Sec. 1129(b)(2) | Eliminates priority for separate class of unsecured creditors. |
| Sec. 502(b) | Amends section 502(b)(7) to delete claims resulting from modification of retiree benefits from the limitation of the section. |
| Added to S.548 | Amends 26 USC 419A(c)(2)(A) and 512(a)(3)(E)(i) to eliminate funding disincentives (New Subsections (g) and (h)). |

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## American Council of Life Insurance

## Amendments to S.548

[ ] deletions from S.548

___ additions to S.548

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Retiree Benefits Security Act of 1987".

Sec. 2. [(a) Section 1113(f) of title 11, United States Code, is amended by inserting "(including any provision relating to benefits for retired employees)" after "provisions" the first place it appears.]

[(b)] (a) Section 1113 of title 11, United States Code, is amended by adding at the end thereof the following:

["(g) Claims arising under any collective bargaining agreement covered by this section, or as a result of the rejection of any such agreement, shall not be limited by section 502(b)(7) of this title.]

"(g) ["(h)] The labor organization which is the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section is, for purposes of this section, the authorized representative of those persons receiving any retirement benefits covered by such agreement, unless such labor organization elects not to serve as the authorized representative of such persons.

"h" ["(i)] In cases where the recognized exclusive collective bargaining representative of the unit or units of employees covered by a collective bargaining agreement covered by this section elects not to serve as the authorized representative of those persons receiving any retirement benefits covered by such an agreement, the court, upon motion of such persons, and after notice and hearing, shall appoint a committee of retired employees, from among such persons, to serve as the authorized representative of such persons, under this section". Notwithstanding any other provision of law, a retired employee so serving, shall not be liable for any action taken or lack of action by such person as a member of such committee in good faith and with reasonable diligence.

c. Subchapter I of Chapter 11 of title 11, United States Code, is amended by adding at the end thereof, the following new section :

"Sec. 1114. Payment of benefits to retired employees

"(a) For purposes of this section, the term 'retiree benefits' means benefits for retired employees and their spouses and dependents, under any plan, fund or program maintained or established in whole or in part by the debtor prior to filing a petition commencing a case under this title (through the purchase of insurance or otherwise) for the purpose of providing medical, surgical, or hospital care benefits, or benefits in the event of sickness, accident, disability, or death.

"(b) For purposes of this section, the term 'authorized representative' means the authorized representative designated pursuant to subsection [(h)] (g) or [(i)] (h) of section 1113 of this title, or, in the case of recipients of retiree benefits not covered by a collective bargaining agreement covered by section 1113, the authorized representative appointed pursuant to subsection (c) of this section.

"(c) The court, upon motion of recipients of retiree benefits not covered by a collective bargaining agreement covered by section 1113 of this title, and after notice and a hearing, shall appoint a committee of retired employees from among such persons to serve as the authorized representative of such persons under this section. Notwithstanding any other provision of law, a retired employee so serving, shall not be liable for any action taken or lack of action by such person as a member of such committee in good faith and with reasonable diligence.

"(d)(1) Notwithstanding any other provision of this title, the debtor in possession, or the trustee if one has been appointed under the provisions of this Chapter (hereinafter in this section 'trustee' shall include a debtor in possession), shall pay or continue to fund and shall not modify any retiree benefits to or for the benefit of retired employees and their spouses and dependents, whether or not such retiree benefits are covered by a collective bargaining agreement covered by Section 1113 of this title [except that] for a period of 60 days after the date of the filing of the petition. Thereafter, ---

> "(A) the court, on motion of the trustee, and after notice and a hearing, may order modification of such payments, pursuant to the provisions of subsections (e) [,] and (f) [and (g)] of this section, or subsection (e) of section 1113 of this title, or
>
> "(B) the trustee and the authorized representative of the recipients of those benefits may agree to modification of such payments,

after which such funding or payments as modified shall continue to be paid by the trustee until the plan is confirmed or the case is dismissed.

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(2) If the said payments are modified pursuant to subsection (d)(1)(A) of this Section 1114, then each person entitled to retiree benefits shall have the option to purchase, at group rates if available, insurance to replace any diminution of coverage caused by the modification. If the payment of any retiree benefits provided by the estate is covered by insurance, then the trustee shall make such payments of premiums and other charges as are necessary to keep such insurance current at all the times during the pendancy of the case.

["(2) Any payment required to be made by any provision of this section after the date of the filing of the petition and before a plan confirmed under section 1129 of this title is effective has the status of an allowed administrative expense as provided in section 503 of this title.]

"(e) With respect to retiree benefits including those covered by a collective bargaining agreement covered by Section 1113 of this title, the court, pursuant to subsection (d)(1)(A) of this section 1114, upon motion of the trustee, and after notice and a hearing, shall enter an order providing for modification in the payment of such retiree benefits, only if the court finds that -----

"(1) the modifications in the retiree benefits sought by the trustee are necessary to permit the reorganization of the debtor and assure that all creditors, the debtor, and all of the affected parties are treated fairly and equitably; and

"(2) the balance of the equities clearly favors the entry of an order authorizing the trustee to modify the retiree benefits to the level sought by the trustee;

except that in no case shall the court enter an order providing for a modification lower than the level described in paragraphs (1) and (2).

["(f) With respect to retiree benefits that are covered by a collective bargaining agreement covered by section 1113 of this title, and only after such an agreement is rejected under such section, the court, upon motion of the trustee, and after notice and a hearing, shall enter an order providing for such modification in the payment of such retiree benefits as the court finds --

"(1) is necessary to permit the reorganization of the debtor and assures that all creditors, the debtor, and all of the affected parties are treated fairly and equitably; and

"(2) is clearly favored by the balance of the equities,

except that in no case shall the court enter an order providing for such modification which provides for a

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**modification to a level lower than that proposed by the trustee in the proposal found by the court in the section 1113 proceeding to have complied with the requirements of subsections (b) and (c) of section 1113.]**

"(f) [(g)](1) Prior to a court issuing a final order under subsection (e) of this section **but only after the expiration of the 60 day period provided by subsection (d)(1) of this section 1114**, if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may authorize the trustee to implement interim changes in retiree benefits **whether or** not provided by a collective bargaining agreement covered by section 1113 of this title.

"(2) Any hearing under this subsection shall be scheduled in accordance with the needs of the trustee.

"(3) The implementation of such interim changes does not render the motion for modification moot.

(g) ["(h)] In calculating the amounts of the claims for unpaid future retiree benefits, or for any retiree benefits not provided due to modifications authorized pursuant to this section, and in calculating the amounts payable pursuant to any plan for such claims, any retiree benefits paid between the filing of the petition and the time a plan confirmed under section 1129 of this title becomes effective shall not be deducted or offset from such amounts unless otherwise agreed by the [debtor] trustee and the authorized representative of the recipients of those retiree benefits.

["(i) No claim for retiree benefits shall be limited by section 502(b)(7) of this title.]

(d) Section 1122 of title 11, United States Code is amended ---

[(1) in subsection (a), by striking out "subsection (b)" and inserting in lieu thereof" subsections (b) and (c)"; and]

[(2)] by adding at the end of subsection (b) thereof the following:

["(c) A plan shall place a] "All claimants for retiree benefits (as such term is defined in section 1114), [in a separate class consisting only of such claimants".] shall be members of this class.

[(e) Section 1129(b)(2) of title 11, United States Code, is amended by ---

(1) redesignating subparagraph (C) as subparagraph (D); and

(2) inserting between subparagraph (B) and subparagraph (D), as redesignated herein, the following:

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"(C) With respect to a class of claimants for retiree benefits (as such term is defined in section 1114) ---

"(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim, property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

"(ii) the plan provides that each holder of a claim of such class receive such value as found by the court to represent the minimum reduction in retiree benefits consistent with the ability of the debtor or provide such retiree benefits after confirmation of the plan".]

(e) Section 502(b) of title 11, United States Code, is amended by- -

adding in subsection (7) thereof after the word "contract" the first time it appears, the following:

"other than a claim resulting from the termination or modification of retiree benefits as defined in section 1114(a) of this title";

(f) The table of sections for subchapter I of chapter 11, title 11, United States Code, is amended by adding at the end thereof the following new item:

"1114. Payment of benefits to retired employees".

(g) Subparagraph (A) of Section 419A (c)(2) of title 26, United States Code, is amended by striking out "(determined on the basis of current medical costs)" and inserting in lieu thereof "(determined on the basis of current and reasonably anticipated future medical costs)".

(h) Clause (i) of Section 512(a)(3)(E) of title 26, United States Code, is amended by striking out "(not taking into account any reserve described in section 419(A)(c)(2)(A) for post-retirement medical benefits)."

[(g)] (i) This Act and the amendments made by this Act other than the amendments to title 26, United States Code, shall become effective on the date of enactment of this Act and shall be effective with respect to cases commenced under chapter 11 of title 11, United States Code, in which a plan for reorganization has not been confirmed by the court as of October 2, 1986, and in which any retiree benefit, as defined in section 1114 of title 11, United States Code, is still being paid on October 2, 1986 or thereafter, and in cases that become subject to chapter 11, title 11, United States Code, after October 2, 1986. The amendments to title 26, United States Code, made by this Act, shall become effective for taxable years beginning on or after the date of enactment of this Act.

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# PREPARED STATEMENT OF FREDERIC G. BURKE

The following statement is submitted by Frederic G. Burke, a Senior Vice President of The National Bank of Washington, a national banking association located in Washington, D.C. -- hereafter referred to as "NBW".

NBW is the trustee under a 1947 Indenture pursuant to which Jones & Laughlin Steel Corporation, a company that was merged into LTV Steel Company, Inc. in 1984, issued various bonds. Although the bonds are secured by certain assets of LTV, it is unclear at the present time whether the value of the collateral securing the bonds is sufficient to cover the entire amount that is owed to our bondholders. To a large extent, the collateral for the bonds consists of old Jones & Laughlin Steel Company facilities which are either completely closed or are operating marginally. Presently, there is approximately 330 million dollars of these bonds outstanding. As the trustee for these bondholders, NBW represents one of the largest claims in the LTV cases.

While the aggregate amount of the bondholder claims is large, in many instances the bonds themselves -- some of which are in denominations as small as $1,000 -- are held by individuals who often times are elderly, retired or of modest means.

It doesn't take an exceptional memory to recall the days when people thought there was no safer place for one's retirement nest egg than steel industry bonds. These bondholders, many of whom invested their life savings years ago, have now had a painful and devastating awakening.

Since the filing of LTV Steel's bankruptcy petition, bondholders have not received any payments whatsoever and they face the prospect of not receiving payments for years to come.

Because of its statutory duty to protect the bondholders, NBW is greatly concerned by Senate 548, "The Retiree Benefits Security Act of 1987". NBW is particularly concerned with that provision of the act which grants an administrative expense priority under the bankruptcy code to certain retiree benefits. Specifically, Senate 548 provides that payments which are required for retiree benefits during the period after the date of the filing of the bankruptcy petition and before a plan of reorganization becomes effective are to be treated as administrative expenses as provided in Section 503 of the Bankruptcy Code. Under the existing provisions of the Bankruptcy Code, such administrative expenses are generally accorded the first priority in payment among unsecured claims.

In the past, administrative expense priorities have been granted either to the actual and necessary costs and expenses of preserving the bankruptcy estate or to charges arising from services that result in a benefit to the bankruptcy estate. As such, the administrative expense priority has a twofold purpose. First, employees, trade suppliers and others are encouraged to continue to do business with a debtor in order to help it reorganize. Second, creditors and others are encouraged to actively participate in the bankruptcy process, again in an effort to rehabilitate the company. Because the incurrence of administrative expenses results in a tangible benefit to all parties involved in a bankruptcy case, Congress has granted such expenses the first priority in payment.

In contrast, the payment as an administrative priority of retiree benefits, inasmuch as they arise from services that may have been rendered many years prior to the filing of a bankruptcy petition, does not yield the same type of direct benefit to the debtor, its creditors, employees, and other interested parties. By granting retiree claims a first priority, Senate 548 provides for the total reordering of a longstanding system of bankruptcy priorities and creates a preference for one group of prepetition unsecured creditors over other groups that are equally deserving. As desirous as it may be to assist retirees who have been hurt by a bankruptcy filing, the fundamental bankruptcy policy of Equality of Distribution should not be abandoned so as to favor one group of legitimate claimants -- the retirees -- at the expense of other legitimate and devastated claimants, such as bondholders.

As this committee knows, the bankruptcy law has recently undergone thorough reviews by Congress when it passed both the Bankruptcy Reform Act of 1978 and the Bankruptcy Amendments and Federal Judgeship Act of 1984. These statutes continue intact a policy of limiting the administrative expense priority to services that directly benefit the bankruptcy estate -- a policy which can be traced back as far as the Bankruptcy Act of 1867.

Viewed just in the context of the LTV cases, the effect of the reordering of priorities contemplated by Senate 548 is enormous. Annual payments for retiree benefits in those cases alone are estimated to exceed many millions of dollars. The impact of moving these claims to the "front of the line" will have a the major negative effect on the bondholders and other claimants.

Not only does Senate 548 represent a radical departure from longstanding bankruptcy principles of Equality of Distribution, but it may also have the unintended consequence of providing retirees with fewer long term benefits than they would otherwise have received.

Under the Bankruptcy Code, in order for a plan of reorganization to be confirmed, administrative expenses must generally be paid, in cash, in full, on the effective date of the plan. By requiring a financially distressed company such as LTV, to make additional, up front, cash payments for certain retiree benefits in order to confirm its plan of reorganization, Senate 548 will necessarily place a substantial added financial burden on Chapter 11 debtors. No doubt, some Chapter 11 debtors will be unable to meet this burden and they will instead be forced into Chapter 7 proceedings, where their assets will be liquidated by a trustee. In such an instance, the very purpose behind Senate 548 - namely the protection of retiree benefits -- would be thwarted since, in Chapter 7, there is no surviving reorganized company which continues to provide those benefits to retirees.

In submitting this statement, I would like to note that I, personally, and NBW, as an institution, are in full sympathy with the plight of the retirees whose benefits are at risk due to the bankruptcy of their former employers. As a former lawyer with the Department of Labor, I have personal knowledge of how important such benefits are and how devastating their loss can be. However, despite that knowledge, neither I nor NBW can endorse a bill which drastically alters the fundamental bankruptcy principle of equality of distribution by reworking the time tested system of priorities in order to benefit one particular, albeit needy, group of creditors at the expense of other creditors that are equally needy -- especially in circumstances where the cure proposed by Senate 548 may result in additional harm to the very group that it seeks to protect.

## CORRESPONDENCE

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HARVARD LAW SCHOOL
CAMBRIDGE · MASSACHUSETTS · 02138

March 13, 1987

Senator Howard Metzenbaum
Senate Russell Office Building, Room 140
Washington, D.C. 20510

Dear Senator Metzenbaum:

I have read a copy of S.548 as it appeared a few days before you introduced it. I wrote to Judith Bailey at the House Judiciary Committee at her request to note some suggestions for technical improvements and I have sent a copy of that letter to David Starr of your staff at his request.

But basically I believe that your bill is correct in the assumption that the termination of retirement benefits of employees of Chapter 11 debtors, whether or not those benefits are based on collective bargaining contracts, should be dealt with as an amendment to the Bankruptcy Code rather than as separate federal labor legislation.

The matters dealt with in your legislation are confined to the treatment of retirement benefit claims in the bankruptcy case: whether they are based on collective bargaining contracts or on other contracts which can be rejected as executory contracts in bankruptcy; who can represent the retirees in the negotiations required by §1113 of Chapter 11; the claims arising for retirees from the rejection of contracts and their priority; the classification of such claims; and the treatment of such claims on a cram-down under §1129(b).

All of these are matters that arise only in the bankruptcy case and should be dealt with in the Bankruptcy Code which will govern that case and not in other legislation. The approach taken in your bill is perfectly consistent with the approach taken in the enactment of the new Bankruptcy Code in 1978. All rules to be applied only in bankruptcy were contained in the Bankruptcy Code although in some instances that involved removing them from other federal legislation.

Sincerely,

Vern countryman

National Steel

National Steel Corporation
20 Stanwix Street
Pittsburgh, PA 15222
(412) 394-4100

April 8, 1987

The Honorable Howard M. Metzenbaum
140 Russell Office Building
Washington, DC 20510

Dear Senator Metzenbaum:

I would like to assure you of the support of National Steel Corporation for Senate Bill S-548. Depriving retirees of hard-earned health and welfare benefits at the time in their lives when these benefits are most needed is one of the harshest results of a Chapter 11 bankruptcy under current law.

The attainment of substantial equality between retirees and represented employees with respect to such benefits is a desirable legislative goal. Making such benefits an administrative expense and requiring that any reduction thereof be subject to the requirements applicable to changes in a collective bargaining agreement accomplishes that goal.

That goal is also consistent with National Steel's position that companies emerging from Chapter 11 should be prevented from bailing out of huge pension obligations to their retired employees. Assumption of those obligations by the Pension Benefit Guaranty Corporation only weakens that institution and permits the emerging company to unfairly compete with companies such as National Steel who have diligently funded their pension obligations.

We will shortly be proposing legislative solutions to this problem and will present them for your consideration and support.

Sincerely,

Howard M. Love
Chairman of the Board

HML:mlm

4340 Connecticut Avenue, NW
Washington, DC 20008

Telephone
202 537 2167

Frederic G. Burke
Senior Vice President
and Group Manager

The National Bank
of Washington

April 27, 1987

The Honorable Howell T. Heflin
Chairman
Subcommittee on Courts and Administrative Practice
U.S. Senate Committee on the Judiciary
223 Hart Senate Office Building
Washington, D.C. 20510

Dear Senator Heflin:

I am taking the liberty of sending you a copy of the statement I submitted for inclusion in the record of the April 24 hearing before the Subcommittee on Courts and Administrative Practice. The National Bank of Washington (NBW) is a member of the LTV Unsecured Creditors Committee and, therefore, is interested in the "Retiree Benefits Security Act of 1987" which was the subject of the April 24, hearing as well as one held on April 1st.

It appears that NBW's claim in the LTV bankruptcy on behalf of LTV bondholders is second in size only to the claims of the Pension Benefit Guaranty Corporation. NBW consequently has a direct interest in the situation as the representative of thousands of Americans who hold LTV bonds.

Your attention to the points raised in my testimony is appreciated. If you have any questions with regard to our views, I would be happy to respond. NBW looks forward to working with Congress and the Administration to reach a satisfactory solution to this difficult problem.

Sincerely,

Frederic G. Burke
Senior Vice President and Group Manager

FGB:cb
Enclosure

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National Federation of
Independent Business

**NFIB**

April 30, 1987

Honorable Howell T. Heflin
Chairman, Senate Subcommittee
on Courts & Administrative Practice
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

On behalf of the over 500,000 small business owners who belong to NFIB, I am writing to express concern over the impact on small firms of S. 548, the "Retiree Benefits Security Act of 1987". I understand the Senate Judiciary Committee's Subcommittee on Courts and Administrative Practice is currently holding hearings on the bill, and NFIB would appreciate your including this letter in the hearing record.

Small business owners have long been a victim of complex and overly-lenient aspects of our bankruptcy laws. These firms most often fall into the unsecured creditor class which, of course, is the last class in line in the preference payments scheme of Chapter 11.

Certainly, there are reasons for placing secured creditors ahead of those who sell services or goods with the risk of unsecured credit. But unsecured credit sales are also the primary method of operation for small firms engaged in business transactions involving the sale of goods and services. These firms represent the majority of the operating businesses in this country, and they are the primary generators of new jobs in our economy. Yet, one or two bankrupt customers can result in extreme difficulties and, in some cases, business failure for them as well.

The goal of Chapter 11 proceedings is to provide an equitable distribution of the funds available for creditors following reorganization of the bankrupt company. From the small business perspective, however, the funds often do not stretch far enough to cover the debts they are owed, or where they do, the recovery is substantially reduced or completely absorbed by legal fees incurred in the bankruptcy proceedings.

Small firms often operate on the margin. They do not have the resources available to larger competitors to absorb the high administrative and legal costs incurred in attempting to recoup money under Chapter 11.

The delegates to the 1986 White House Conference on Small Business included reform of the bankruptcy laws in their final top 60 recommendations. Recommendation #37 calls for modifying federal bankruptcy laws by:

a. restructuring the preferred payment rules;
b. placing strict controls on the financial dealings of Chapter 11 "Debtor-in-possession" cases;
c. creating a review procedure for trustees to assure that creditors obtain timely financial reports of the bankruptcy operational reports and to avoid self-dealing and patronage;
d. providing equitable reimbursement to creditors from future earnings of debtor;
e. limiting lawyers' participation to the same as other creditors;
f. establishing a bankruptcy ombudsman to make sure that small business creditors are treated fairly; and
g. providing a first priority lien to an unpaid seller of a product or a right to recover the product.

S. 548 deals with problems of nonpayment incurred by another group of unsecured creditors, i.e. retirees. The answer to their problems, in the view of this bill, is to mandate that these retirees, as parties to collective bargaining agreements, be paid. The impact of this requirement may answer concerns for this particular group, but it does nothing to address the concerns of others in similar unfair situations. In fact, by abandoning the basic principle of equitable distribution upon which our bankruptcy laws are intended to operate, S. 548 only exacerbates the problems of other unsecured creditors. Small firms already face problems of being squeezed out by more powerful creditors with greater resources to recoup payments due them. This bill will simply create another class of super-preferred creditors, putting small businesses at an even further disadvantage.

In considering this legislation, we urge the Committee to consider approaches which focus more on the root of the problem for retirees -- that is, insufficient insurance for retiree benefit plans. The approach of S. 548, in our opinion, will simply put additional strain on the already strained bankruptcy system.

We would also urge the Committee to undertake a more comprehensive look at how Chapter 11 bankruptcies are working. From the viewpoint of small business, the retired workers are not the only ones denied payment due them under the current system.

Sincerely,

John

John J. Motley III
Director
Federal Governmental Relations

**National Intergroup, Inc.**
Government Affairs
1575 I Street NW, Suite 1100
Washington, D.C. 20005
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**William D. Thompson**
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NATIONAL
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The Honorable Howell Heflin
Chairman
Subcommittee on Courts and
Administrative Practice
223 Hart Senate Office Building
Washington, D.C. 20510

Dear Senator Heflin:

I am writing to emphasize the support of National Steel Corporation for S. 548, the Retiree Benefits Security Act of 1987. As you know, this legislation is currently pending in the Subcommittee on Courts and Administrative Practice of the Committee on the Judiciary of the United States Senate. The Subcommittee received testimony at hearings conducted on April 1, 1987, and April 24, 1987. That testimony raised a number of concerns with the legislation which I believe can be effectively and conclusively addressed.

Certain individuals have suggested that the role of the bankruptcy law as social legislation is inappropriate. I would strongly suggest that the bankruptcy law is inherently social legislation because it deals with the social problems created by insolvent individuals and businesses. Over the years, the bankruptcy law has been amended to accommodate emerging social considerations. The most recent example concerns amendments to the bankruptcy law dealing with farmers. The problems addressed by S. 548 are ones which the country now recognizes to be of great national importance. The suffering incurred by retirees who lose hard earned health and welfare benefits cannot be understated. It is precisely the type of problem which Congress is most able to address.

Some have suggested that amending the bankruptcy law in the manner set forth in S. 548 would unfairly favor retirees as creditors. I would submit that it is essential to provide retirees special status under the Bankruptcy Act because these individuals are least able as creditors to protect their own interests in an effective manner. The loss of their health and welfare benefits would impose a catastrophic consequence on them which cannot be addressed through later negotiations. The normal creditor often has an ongoing relationship with the debtor in possession as a trade creditor or a lending institution. Through future business dealings these entities have various ways of dealing with their concerns. Retirees who have suffered a loss of their health and welfare benefits have no similar negotiating position. The potential consequence to the Federal government of failing to address the loss of health and welfare benefits in this manner could be the imposition of a significant financial burden ultimately at the Federal level, a distinctly unpalatable prospect given our current fiscal and budgetary problems.

Certain suggestions have been made that S. 548 should not be applied to pending bankruptcies. I would strongly submit that there are two compelling reasons which clearly support the application of this legislation to pending bankruptcies. First, the failure to apply these rules to pending bankruptcies would impose human suffering on a large class of retirees who are being affected by a variety of pending bankruptcies, e.g., LTV Corporation, Wheeling Pittsburgh, Kaiser, and A.H. Robbins. For this reason alone, S. 548 should be applied to pending bankruptcies.

An equally compelling reason exists for applying this legislation to pending bankruptcies. Specifically, it concerns the overall competitive balance within our nation's steel industry. Currently, the U.S. steel industry can be divided into three classes. In the first class are those companies which currently are in bankruptcy. These include LTV Corporation, Sharon Steel, Wheeling Pittsburgh, and Kaiser. In the second category are those companies which are considering the possibility of filing for Chapter 11 protection. In the third category are those companies which are financially well managed and strong and which are not currently contemplating Chapter 11 protection.

If S. 548 is enacted but does not apply to pending bankruptcies, the consequences would be indefensible from a public policy standpoint. First, those companies which are in bankruptcy would receive the benefit of shedding the responsibilities associated with welfare benefits earned by retirees. Combined with the other benefits obtained through the bankruptcy process, this would place these companies in a competitively stronger position than their counterparts who are financially weak but who have not chosen Chapter 11 bankruptcy protection. Second, the possibility that S. 548 may be applied to only future bankruptcies may cause certain companies in the steel industry which are considering bankruptcy to be forced into filing for Chapter 11 protection. The existence of legislation which forces additional bankruptcy cannot be good public policy. Third, failure to apply this legislation to pending bankruptcies would have a counterintuitive policy result. It would provide a tremendous benefit to those companies which were poorly managed but able to acquire Chapter 11 protection prior to the effective date of the legislation while competitively penalizing both (1) those financially weak steel companies which have not chosen Chapter 11 and (2) those financially healthy steel companies who will be forced to compete with steel companies who were able to elect chapter 11 status prior to the effective date of the legislation.

The competitive concerns raised here extend beyond the obligations of Chapter 11 companies for health and welfare benefits of retirees. In addition, the pension liabilities which these companies have successfully shifted to the Pension Benefit Guaranty Corporation raises further competitive concerns for the entire U.S. steel industry. Likewise, the ability of Chapter 11 companies to avoid payment of dividends and interest further exacerbates the competitive concerns which exist within the industry. These are all concerns which National Steel is reviewing in greater detail. In the meantime, I would strongly urge the enactment of this legislation on a basis which applies it to all pending bankruptcies to avoid the potential competitive imbalance inherent in providing relief from these health and welfare obligations to certain members of the steel industry and not to others.

Sincerely,

William D. Thompson
William D. Thompson
Vice President